**Chuck Quackenbush**
Insurance Commissioner

November 1999

To All California Consumers:

It is my pleasure to present this *Report of Accomplishments* summarizing the achievements of the California Department of Insurance (CDI) from 1995 to 1998.

When comparing today to where we were in 1995 it is important to note that the California insurance market was a very different place. The Northridge earthquake in 1994 was the latest in a string of natural disasters that utterly devastated the homeowner and earthquake insurance markets and brought the entire California industry to the brink of collapse. To make matters worse, auto insurance was among the most expensive in the nation and insurance providers were leaving California in droves in search of a friendlier business climate.

In contrast, the accomplishments contained in this report translate into tremendous benefits to California's consumers in several critical areas:

- Successfully decreasing the cost of auto insurance.
- Providing greater access to information about insurance.
- Encouraging greater access to insurance in under-served communities.
- Making essential insurance products, particularly homeowner's, earthquake, and health care insurance for small businesses, more available.
- Ensuring better protection against unfair and illegal insurance practices.
- Providing better protection against insurer insolvency.
- Enhancing the efficiency and effectiveness of CDI's operations.
- Intensifying efforts to promote social justice in holocaust-era claims payments.

The significance of this report is not that we have made insurance problems less of a civic concern than other problems; but rather, the significance is that we have accomplished making the insurance market stable, competitive and efficient without excessively burdensome government meddling. This report reflects a successful alliance of business and government working in tandem to serve the needs of *all* Californians.

The last four years have been challenging, but extraordinarily productive. This *Report of Accomplishments* is the direct result of the dedication and commitment to quality by every member of the CDI team. As you will read, California's consumers today enjoy a more stable, effectively regulated insurance market that is increasingly more competitive and affordable than ever before.

This is not accidental. It is simply the application of tried and true principles of protecting the consumer, providing a "level playing field" for the insurance industry, getting rid of the "bad actors," and getting government out of the way to let the market flourish. The results are consistently predictable – consumers benefit by having access to products that are a fair value for a fair price, the industry benefits by having an opportunity and incentive to prosper, and the State of California benefits by the generation of tens of thousands of jobs *and* by the substantial investment being injected daily into the economy. This is the vision that has successfully guided CDI for the last four years.

This *Report of Accomplishments* will also serve as the foundation for CDI's future innovation and achievement in the area of insurance regulation and consumer protection. As such, we will continue to shape CDI into a model of "good government" that we can all be proud.

Numerous individuals have contributed to the many successes during my first term as Insurance Commissioner. Their work has resulted in significant, positive advancements for California's consumers and they deserve the credit and my sincerest gratitude. I want to particularly thank the past and present members of my Executive Management Team, whose persistent leadership has been instrumental in these achievements.

Sincerely,

**CHUCK QUACKENBUSH**
Insurance Commissioner

## *Commissioner's Mission Statement*

*Our mission is to ensure that consumers are protected against unfair practices, excessive or discriminatory insurance rates, and insurer financial instability; that the laws are enforced with equal diligence; that all consumers are served in the most efficient, responsive manner; and that the regulatory process is open, fair, and equitable.*

***– Chuck Quackenbush***
*California Insurance Commissioner*

# REPORT OF ACCOMPLISHMENTS
# 1995 - 1998
# *"PROTECTING CALIFORNIA'S CONSUMERS"*

## TABLE OF CONTENTS


**I. EXECUTIVE SUMMARY .......... 1**

**II. THAT WAS THEN…*THE CHALLENGES FACING CDI IN 1995* .......... 4**

MAJOR POLICY CHALLENGES .......... 4

*Incomplete Implementation of Prop. 103 .......... 5*
*State of Crisis in Essential Insurance .......... 5*
*Limited Access to Affordable Healthcare .......... 5*
*Lack of Investment in California's Low-Income and Minority Communities .......... 5*
*Declining Competitiveness in the Market .......... 5*
*Inadequate Responsiveness to Consumers .......... 5*
*Conservation and Liquidation Office .......... 6*

CDI'S INTERNAL CAPACITY PROBLEMS .......... 7

*Consumer Services Branch .......... 7*
*Enforcement Branch .......... 7*
*Fraud Branch .......... 7*
*Financial Surveillance Branch .......... 7*
*Legal Branch .......... 7*
*Rate Regulation Branch .......... 8*
*Administration Branch .......... 8*

**III. …THIS IS NOW! 1995 - 1998 .......... 9**

SIGNIFICANT AUTO INSURANCE REFORMS .......... 9

*Implementation of Proposition 103 .......... 9*
*Legislative Initiatives .......... 12*
*Innovative Automobile "Mini-Policy" .......... 13*

EXPANDED ACCESS TO INSURANCE INFORMATION .......... 14

*Award-Winning CDI Web site .......... 14*
*Consumer Outreach .......... 15*

IMPROVED INSURANCE MARKET .......... 16

*Restored Stability in the Homeowner's Insurance Market .......... 16*
*The Cutting Edge - California Earthquake Authority .......... 17*
*Broadened Access to Health Insurance .......... 19*

AGGRESSIVE ENFORCEMENT ACTIONS .......... 21

*Protecting California's Consumers .......... 21*
*"Consumer Alert" .......... 23*
*Strengthened Surplus Lines Regulation .......... 24*
*Reinforced Consumer Services Division .......... 24*

CRACK DOWN ON INSURANCE FRAUD ........ 26

*Enhanced Anti-Fraud Capabilities ........ 26*
*Extensive Anti-Fraud Outreach Efforts ........ 26*
*Initiated "Operation Storm Watch" ........ 26*
*Fraud's "Most Wanted" ........ 27*
*Workers' Compensation Fraud ........ 27*
*Increased Enforcement and Deterrence Against Auto Fraud ........ 28*
*Increased Enforcement and Prosecution of Other Types of Fraud ........ 29*

CDI'S EFFICIENCY AND EFFECTIVENESS ........ 31

*Instituted the Consumer Ombudsman as Problem-solver for the Public ........ 31*
*Modernized CDI Consumer's "Hotline" ........ 31*
*Improved Administrative Responsiveness ........ 32*
*National Leadership in Insurance Regulatory Improvements ........ 37*

CONSUMER PROTECTION ........ 38

*Restoring the Conservation and Liquidation Office ........ 38*
*Innovative De-mutualization Efforts ........ 39*

INTERNATIONAL EFFORTS FOR HOLOCAUST SURVIVORS ........ 41

*The Significance of this Effort ........ 41*
*California's Responsibility to Restore Benefits for Holocaust Survivors ........ 42*

HELPING URBAN COMMUNITIES ........ 44

*Efforts to Spur Insurance Involvement in Urban Areas ........ 44*
*The Commissioner's Report on Under-served Communities ........ 44*
*California Organized Investment Network ........ 44*

***APPENDIX ........ 46***

# I. EXECUTIVE SUMMARY

The California Department of Insurance (CDI) regulates the largest insurance market in the United States and one of the largest in the world.

The office of the Insurance Commissioner was established by act of the California State Legislature in 1868, coincident with the enactment of the first comprehensive statutory regulation of the business of insurance in California. The position was a Governor's appointment. However, in 1990 California voters approved Proposition 103. One of the provisions of the Proposition provided that the People shall elect the "Commissioner" at the same time, place and manner for the same term as the Governor (every four years).

The Insurance Commissioner is vested full power, authority and duty to enforce the insurance law found in the California Insurance Code.[1] The role of the Insurance Commissioner is to regulate the insurance industry thereby protecting consumers of California from abusive insurance practices. Listed below are some of the various duties imposed upon the Insurance Commissioner of the State of California:

1. Investigation of complaints and respond to inquiries by consumers.
2. Qualify and license companies interested in providing insurance products.
3. Examination of the business and affairs of insurance companies.
4. Administer the conservation and liquidation of insolvent and delinquent insurance companies.
5. Licensing and regulation of insurance producers.
6. Review and approval of insurance rates.
7. Combating insurance fraud.
8. Collection of fees, reimbursements, fines and penalties from the insurance industry.

CDI's primary responsibility is to protect California's insurance policyholders. To accomplish this, the Department maintains 16 offices in several regions and cities in California, including:

- Sacramento (3)
- Los Angeles (2)
- Martinez
- San Diego (2)
- Orange County
- Santa Ana
- San Francisco
- San Jose
- Fresno
- City of Commerce (2)
- Rancho Cucamonga

[1] California Insurance Code Section 12921

The California Insurance Code remains the primary directive for the Department. The Insurance Code mandates that CDI administer and execute various programs for the protection of California's citizens:

- **Regulation of Insurance Companies and Insurance Producers –** to protect the public from insurer insolvency or discriminatory, unlawful, or fraudulent practices.
- **Consumer Protection –** to protect California consumers against unfair practices and excessive or discriminatory insurance rates.
- **Fraud Control –** to control insurance fraud by conducting investigations and preparing fraud cases for prosecution.
- **Tax Collection and Audit –** to perform insurance tax audits, propose tax adjustments, and monitor collections in the process of assisting the Board of Equalization in determining various refund and assessment matters.
- **Earthquake Grants and Loans –** to provide residential grants and loans to retrofit high-risk residential dwellings owned or occupied by low to moderate income households.
- **Administration –** to provide policy direction of CDI from the Commissioner's Office.

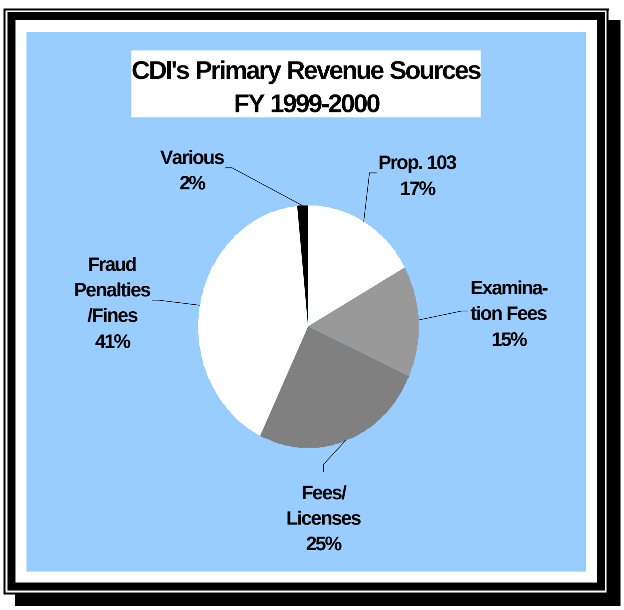
In order to execute the Insurance Code's objectives, the Department has over 1,000 employees organized into eleven distinct branches, including:

- **Legal Branch –** provides legal review and analysis of CDI enforcement actions and policy approvals and promulgates regulations.
- **Administration Branch –** provides internal support to ensure CDI operational efficiency.
- **Fraud Branch –** investigates and deters criminal fraud activity.
- **Rate Regulation Branch –** ensures fairness of rate applications by insurers.
- **Consumer Services & Market Conduct Branch –** performs market conduct examinations of insurers and assists consumers.
- **Financial Surveillance Branch –** monitors the financial status of the insurance industry.
- **Enforcement Branch –** protects consumers by enforcing existing insurance laws and regulations.
- **External Affairs & Policy Branch—**supports consumers through legislative advocacy and research of various initiatives.

- **Executive Programs Branch –** coordinates special projects and policy initiatives as directed by the Commissioner – includes the Office of the Ombudsman and the California Organized Investment Network (COIN).
- **Strategic Planning Branch –** oversees strategic planning and implementation of goals and objectives of the Department of Insurance to maximize all areas of operation – from communications and policy development to legislation, public appearances, statements/speeches, and agenda formulation.
- **Press and Publications Office –** provides information to the public and the media about the Department's mission to protect California consumers.

The Department of Insurance is funded through a variety of different revenue streams. Overall, the Department administers a $136 million budget. CDI's traditional funding sources total approximately $121 million. *Exhibit 1* illustrates the Department's revenue breakdown by major funding source.

***Exhibit 1:CDI's Primary Revenue Sources, FY 1999-2000***




Source: California Department of Insurance, Budget Office, 1999.

In addition to the ongoing funding mechanisms outlined above, CDI has also secured additional, provisional funding to support particular initiatives. This revenue totals approximately $14.4 million. *Exhibit 2* outlines this revenue.

***Exhibit 2: Additional Funding Sources, FY 1999-2000***

| Funding Source | Amount ($) |
|---|---|
| Holocaust | $6,364,000 |
| SB 18 (Chapter 239/Aug. 1997) | $3,334,000 |
| Various (Earthquake; General Fund; Title Insurance and Reimbursements | $4,767,000 |
| **Total** | **$14,465,000** |

Source: California Department of Insurance, Budget Office, 1999.

In fulfilling its legislative mandate and public responsibility, the Department continues to pursue funding streams to serve California consumers.

## *Recent History*

In 1995 the California insurance market was in crisis. A major earthquake with a magnitude of 6.7 struck the city of Northridge in Southern California at 4:31 a.m. on January 17, 1994 causing $12.5 billion in *insured* losses. What was left in the wake of Northridge and other recent catastrophic temblors, such as the 1989 Loma Prieta earthquake in Northern California, was an insurance market on the brink of insolvency and utter collapse. This is where this report begins – as it retraces the steps of the California Department of Insurance from 1995 to 1998.

CDI regulates the largest insurance market in the United States, with over $71 billion in direct insurance premiums written in the state. Regulating the activities of this sprawling insurance market is a serious responsibility and a complex challenge, requiring the efforts of teams of staff that conduct investigations, enforce laws and regulations, analyze data, provide customer service, and perform other important duties. In the last several years CDI has been transformed into a national example of how state insurance regulation can be more responsive, efficient and effective in protecting the interests of consumers.

Significant improvements have redeemed this important regulatory agency as it embarked on a voyage of transformation in the insurance industry. Though confronted with an array of complex issues and daunting challenges in 1995, CDI has compiled a substantial record of accomplishments. The fact that the challenges were addressed successfully is due in great part to the commitment of the persistent leadership and staff of CDI.

In 1995, CDI faced:

- Voter mandates in Proposition 103 that had not been implemented.
- Auto insurance was one of the most expensive in the nation.
- Crisis in homeowner's and residential earthquake insurance market.
- Declining competitiveness in the insurance market.
- Questionable management practices and operations at CDI.
- Limited access to affordable healthcare insurance.
- Lack of industry investment in California's low-income and minority communities.

## *CDI's Rebirth*

The last four years have indeed been extraordinarily challenging. Today, however, CDI's performance is much stronger – consumers are better protected; insurance is more affordable; and insurers enjoy a more competitive market. CDI's goal for the next four years is to build on these achievements and ensure that CDI maintains its role as a national leader in effective insurance regulation and consumer protection.

CDI continues to explore new technology to improve responsiveness and continues to streamline processes so that work gets completed more timely and accurately. CDI also continues to focus on aggressive enforcement of insurance laws and punish violators. Also, CDI continues to create a regulatory environment of fairness that encourages insurers to do business in our state, to increase competition and make insurance rates more affordable for consumers. CDI continues to be a model of "good government," benefiting both consumers and insurers.

## *Building on the Record*

Looking forward to the future, CDI will build on the accomplishments of the last four years:

- Lower costs for automobile insurance.
- Greater access to essential insurance products – particularly homeowner's, earthquake, and health care for small businesses.
- More accessible information on insurance.
- Better protection against unfair and illegal insurance practices.
- Improved protection against insurer bankruptcy.
- Enhanced anti-fraud enforcement.
- Improved efficiency and effectiveness of CDI's operations.
- Increased efforts to promote social justice in Holocaust victim restitution.
- Innovative approaches for helping underserved communities.

These are some of CDI's accomplishments during 1995 to 1998. It is with great anticipation that CDI's Executive Management Team and everyone on the team at CDI accept the challenges that lay ahead and diligently strive to take insurance regulation into the 21st Century. ❖

# II. THAT WAS THEN…*THE CHALLENGES FACING CDI IN 1995*

## *Overview of this Section*

### Major Policy Challenges

- *Implementing Proposition 103*
- *Resolving the crisis in homeowner's and residential earthquake insurance*
- *Addressing access to healthcare insurance*
- *Encouraging industry investment in California's low-income and minority communities*
- *Declining competitiveness of the insurance market*
- *Inadequate responsiveness to consumers*
- *Troubled operations: Conservation and Liquidation Office*

### Internal Capacity Issues

- *Enforcement Branch*
- *Fraud Branch*
- *Financial Surveillance Branch*
- *Legal Branch*
- *Rate Regulation Branch*
- *Administration Branch*

## MAJOR POLICY CHALLENGES

In January 1995, CDI was facing significant challenges, not the least of which was the implementation of Proposition 103 – the initiative that radically changed insurance law in California. Although Proposition 103 was approved by the voters in 1988, numerous lawsuits and challenges by insurers and consumer groups delayed its full implementation. By 1995, forced rate reductions and rebates to consumers, and the added expense of doing business in California under Proposition 103's mandates had led to insurance companies leaving the state. The results were a dangerous decline in the competitiveness of the insurance market.

In addition to Proposition 103, CDI faced other challenges, such as reversing a crisis in the homeowner's and residential earthquake insurance market, providing leadership and direction in a national debate over health care insurance, and ensuring that adequate insurance is available to low-income and minority neighborhoods.

To compound the problems, CDI's existing technology infrastructure did not provide the means or the tools to address and solve these issues. The regulatory processes were time-consuming and often mired in backlogs and delays. CDI was understaffed in key areas and several significant problems were identified in audits conducted by state oversight agencies. A number of negative reports publicized CDI's problems in various California newspapers. All in all, the combined affect of these issues had a direct and adverse impact on CDI's quality of services and the protection consumers deserve.

## *Incomplete Implementation of Prop. 103*

In order to fully implement Proposition 103, processes mandated by the initiative needed to be clarified and developed. Steps that still needed to be taken included developing an automated rate comparison system; reformulating the rating factors for auto policies; and enforcing the new Proposition 103 requirement of prior approval of all policies and rates before being be sold to consumers. By 1995, eight years after passage, CDI still had yet to process and enforce the rebate obligations of 185 companies that owed money to California's consumers as a result of the rollbacks dictated by Proposition 103. Due to the complexity of the initiative and the many legal challenges, CDI's commissioners prior to 1995 were unable to implement many provisions of Proposition 103.

## *State of Crisis in Essential Insurance*

1995 was a time of crisis in the California insurance market. The Northridge earthquake had struck just 12 months earlier paralyzing Southern California and causing approximately $12.5 billion in insured losses. What was left in the massive wake of Northridge and other catastrophes, such as the 1989 Loma Prieta earthquake in Northern California, was a fear among insurers that underwriting earthquake risks would jeopardize their financial ability to operate.

Because California law mandates insurers selling homeowner's policies must also offer earthquake coverage, many insurers placed untenable restrictions on new policies. Some insurers simply stopped writing new homeowner's policies at all and refused to renew existing policies as they came up for renewal. As a consequence, tens of thousands of Californian homeowners were unable to maintain such basic and essential protection as homeowner's insurance. Perhaps worse, those attempting to buy homes were unable to obtain lender-required homeowner's insurance and close escrow. The result was that the homeowner's and earthquake insurance crisis was also threatening the viability of California's real estate market and became a drag on the economy as a whole. CDI was receiving an average of 3,000 calls per month from consumers complaining of difficulties in obtaining homeowner's and earthquake insurance.

## *Limited Access to Affordable Healthcare*

During the mid-1990's, Californians not only faced a crisis in essential homeowner's and earthquake insurance they also confronted the national dilemma of obtaining affordable health care insurance. As it is today, healthcare reform was a highly visible, national issue at the end of 1994. In California, CDI was confronted with the problem of small businesses not being able to provide even basic health insurance benefits to employees due to its high cost. The lack of small group health insurance coverage particularly affected consumers who worked for businesses employing less than 20 employees. Finding a solution to bringing down the cost for these policies and providing adequate coverage to make it a value worth purchasing was a significant predicament.

## *Lack of Investment in California's Low-Income and Minority Communities*

At the end of 1994, CDI was still searching for practical ways to encourage insurance companies to invest part of their capital in under-served communities. CDI was at a loss trying to develop any sensible solutions or make any progress bringing insurers to participate in community development investments or to invest a percentage of premium revenues from California residents into investments benefiting low and moderate-income communities.

## *Declining Competitiveness in the Market*

By the end of 1994, California was one of the most expensive auto insurance markets in the nation. Beginning in the early 1990's, many insurers withdrew from the California market, claiming that the terms of Proposition 103 were too onerous and that the business climate was unfavorable. Insurers were also leaving for other reasons, such as the long delays often experienced in getting approvals for new products or for approval of rate filings. By January 1995, there were approximately 2,044 backlogged files, some dating back four years. Corporate applications were bogged down in a time-consuming *Certificate of Authority* process, some sitting stagnant for more than two years. CDI's inefficiencies were impeding the desirable growth of the insurance market. By 1994, 21 companies had given up on California and left the state.

## *Inadequate Responsiveness to Consumers*

By the beginning of 1995, outdated manual processes and inefficient practices were significantly impeding the CDI's responsiveness to consumers and insurance providers alike.

Information from CDI to California's consumers was available only in paper copy. In 1993 alone, CDI shipped 62,463 publications to consumers at a significant cost for document development, reproduction, handling, and postage. CDI had yet to take advantage of automated tools, such as Internet-based methods of communication, to provide enhanced services and information to California's consumers.

The preceding administration acknowledged in November 1994 that CDI had to acquire information technologies "so that consumer responses can be more accurate, factual, and timely."[2] Despite the clear need to use information technologies to improve communication with consumers, CDI had not been successful in its efforts to implement automated tools.

## *Conservation and Liquidation Office*

Often referred to as the Commissioner's *fiduciary* duty, the Conservation and Liquidation Office (CLO) acts as trustee on behalf of the Commissioner in rehabilitating or liquidating an insurer, whichever is most plausible and in the best interest of the stakeholders. This unique function provides a mechanism by which CDI can assume management of an insurer in the event of insolvency or mismanagement of an insurer. The role requires absolute integrity to make sure that insolvencies are mitigated appropriately. By 1995, however, the CLO had been the subject of three management audits by various state agencies and numerous legislative hearings for failing to safeguard the assets of policyholders of bankrupt insurance companies under state supervision. The basic findings were that the CLO was failing in two significant areas:[3]

1. *Its duty to obtain the highest possible return on the liquidated assets of troubled insurers.*
2. *Distributing the proceeds from these liquidations to policyholders.*

Extensive investigative reports by newspapers across California publicized these shortcomings. In fact, *The Sacramento Bee*[4] ran a three-part series on the mismanagement of assets by the CLO, including "private auctions" of assets to state employees at discount prices.

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[2] CDI Administration Transition Document, p. 17, November 1994.
[3] Department of Finance: *Conservation/Liquidation Division Management Letter*, 12/16/92; Department of Finance: *Conservation/Liquidation Division Management Letter*, 3/24/94; State Auditor: *Conservation and Liquidation Division Report*.
[4] *The Sacramento Bee*, February 20-22, 1994.

# CDI'S INTERNAL CAPACITY PROBLEMS

In 1995, several of CDI's vital operations needed drastic improvement. CDI's information technology infrastructure was severely outdated and the CDI's heart and soul – its employees – were struggling to keep up with workload, relying on inefficient manual processes, insufficient staffing levels, uncertain funding, and ineffective tools.

## *Consumer Services Branch*

The Consumer Services Branch serves as the nervous system of CDI – offering valuable advice for consumers through highly-skilled officers and the CDI Consumer Hotline; performing market conduct examinations to ensure the insurance industry operates fairly and legally; and providing an indispensable conduit between consumers and the insurance regulators. Maintaining adequate staffing to ensure that consumer complaints are handled with the utmost care and urgency is an essential function of CDI. Beginning in 1995, budgetary constraints forced reductions in staffing resources to dangerously low levels. This was especially true for the Consumer Services Branch, which had to layoff the majority of the total 89 staff positions CDI was forced to cut. As the workload increased, staff was ill-equipped to respond properly to the complaints against insurers.

## *Enforcement Branch*

The Enforcement Branch is responsible for investigations and enforcing the laws and regulations. Its role is critically important in the protection of consumers. By the end of 1994, the Enforcement Branch was lacking effective automated tools. For instance, the Enforcement Branch's Licensing Bureau relied strictly on an inefficient manual process for administering licensing examinations. In addition, CDI did not have the resources to provide training to investigators and was unable to adequately address insurer and producer fraud.

## *Fraud Branch*

The CDI's Fraud Branch protects consumers by investigating criminal fraud activity. The lure of big payoffs by cheating insurance companies is hard for some to resist. The consequences, however, are that responsible, law-abiding policyholders end up paying millions in extra premiums thus paying for the unscrupulous activities of others. CDI considers the function of the Fraud Branch in tracking down and shutting down criminals committing fraud a top priority. Like the Enforcement Branch, the Fraud Branch faced problems in meeting the workload demands. The Fraud Branch needed a uniform database to facilitate processing, tracking, and analysis of information. In addition, it needed more personnel resources. At the end of 1994, many of its fraud investigators were available only as "limited term positions." To maintain its workload service levels and meet increasing demands, especially in auto insurance fraud and workers' compensation fraud cases, these positions needed to convert temporary positions to permanent positions.

## *Financial Surveillance Branch*

The Financial Surveillance Branch is responsible for overseeing the financial condition of the insurance industry to ensure they can provide the benefits and protection promised to California policyholders. As was the case with other vital functions of the Department, Financial Surveillance faced resource constraints that limited its ability to serve as an effective watchdog. In 1994, several units of the branch were understaffed and experiencing problems with recruiting and retaining staff with specialized skills. Inadequate staffing levels hampered reviews of the most complex elements of insurers' financial reports. Moreover, the branch needed to develop an automated *Early Warning System* to provide advance warning of insurers headed toward insolvency and to provide automated analytical tools for its employees.

## *Legal Branch*

The Legal Branch serves as the backbone of CDI providing legal review and analysis of enforcement actions, policy approvals, *Certificate of Authority* approvals, promulgating regulations, and many more necessary tasks. A team of attorneys and support staff carefully ensure that the insurance industry complies with California's statutes and regulations. The Legal Branch's Policy Approval Bureau was confronted with extensive backlogs. Although the Insurance Code allows insurers to market most insurance policy forms after 30 days of filing with the CDI, many policy filings waiting to be processed were more than a year old. In addition, the Legal Branch also had to formulate and apply Proposition 103 rollback regulations to approximately 185 insurers who had not yet settled their rollback liabilities and fully implemented a case prioritization system. Backlogs and delays in the Legal Branch deeply affected CDI's reputation and effectiveness as a regulator.

## *Rate Regulation Branch*

The Rate Regulation Branch analyzes and approves or denies the prior approval rate filings submitted by insurers. The primary responsibility of the Rate Regulation Branch is to ensure that rate applications by insurers are adequate (sufficient to maintain solvency), not excessive, and not unfairly discriminatory. To complete this task, the Rate Regulation Branch employs highly technical actuaries and other specifically skilled staff. As in the other branches and bureaus, the Rate Regulation Branch was also experiencing issues with the timeliness of its transactions. The branch was not releasing its final decisions on rate filings within statutory time limitations. (Rate filings are ***deemed*** approved after 60 days, unless action is taken by CDI). Additionally, the branch was experiencing delays in processing Proposition 103 rebate obligations for nearly 185 companies.

## *Administration Branch*

The Administration Branch provides the internal support and administrative functions to make sure CDI, as an organization, runs smoothly and efficiently. A 1991 State Controller's Office audit revealed CDI's failure to comply with basic state accounting and internal control standards. By 1994, after three years, the CDI had not reformed its accounting functions, automated its fiscal activities, implemented workload measurements and standards, or developed an operable *Time/Activity Reporting System* (TARS). The need to implement workload measurements and standards and the TARS system was very important in order to provide the CDI with the capability to accurately track productivity, determine the actual cost of regulatory and enforcement actions, and get reimbursed for its costs.[5] In addition, the Administration Branch was responsible for CDI's insufficient information technology resources. Networked computers and software were not standardized, making them difficult to maintain and support. ❖

[5] AB 1395(Chapter 965/Sept. 1994) requires CDI to base service rates and fees charged to the industry on actual costs

# III. …THIS IS NOW! 1995 - 1998

## *Overview of this Section*

**Effective Regulation**

- *Significant auto insurance reforms*
- *Improved access to insurance information*
- *Availability of essential insurance products*
- *Enforcement of abusive and illegal insurance practices*
- *Insurance fraud committed by individuals*
- *CDI efficiency and cost effectiveness*
- *Increased consumer protection*
- *International efforts for holocaust survivors*
- *Innovative approaches for helping under-served communities*

## EFFECTIVE REGULATION

The California Department of Insurance oversees the largest state insurance market in the United States, with over $71 billion in premiums written and the largest number of licensed insurance producers[6] of any state. Between 1995 and 1998, CDI compiled an impressive record of effectively regulating this large and dynamic insurance market and successfully promoted a stable, competitive, and financially sound insurance market that produces widely accessible insurance policies that benefit all consumers.

## SIGNIFICANT AUTO INSURANCE REFORMS

In 1995 California was one of the most expensive auto insurance markets in the nation. Since then, CDI has helped pass major new legislation and embarked on new initiatives that have resulted in the most dramatic auto insurance rate cuts in California history.

### *Implementation of Proposition 103*

Perhaps one of the most challenging and momentous accomplishments was implementing Proposition 103. Although the voters approved Proposition 103 in 1988, by 1995 it still had yet to be fully implemented. This proposition required major changes in California insurance law:

- *First*, it required an automobile insurance rate rollback.
- *Second*, it required that policyholders receive premium refunds based on the rollbacks.
- *Third*, it required insurers to reformulate rates to be based primarily on a driver's safety record, miles driven and driving experience.
- *Fourth*, it required CDI to provide consumers with comparative information on auto insurance rates.

**[6] 190,000 licensed producers as of 1/1/1999.**

## Rate Rollbacks and Premium Refunds

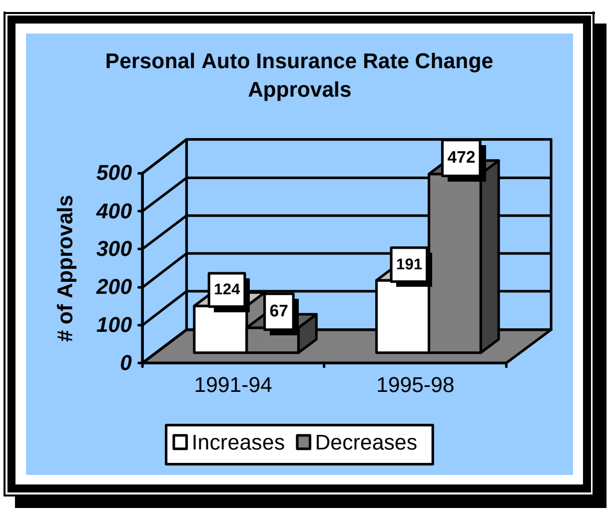
Proposition 103 required insurance companies conducting business in California during 1988 to rollback their rates and pay rebates to consumers based on the difference between their current rates and rollback rates. Not surprisingly, insurers fought rebates and rollbacks vigorously.

In 1995, there were 169 unresolved rate rollback cases, mostly comprised of insurers refusing to rollback their rates. CDI repeatedly fought in the courts to settle these cases and obtain rollbacks and rebates for consumers. In two particularly significant court cases, the Department defended Proposition 103's mandated rollbacks and rebates to consumers. In *Amwest v. Wilson*, the California Supreme Court agreed with the Department's argument that surety companies are not exempt from Proposition 103 regulations and that they are to be governed by the same rate rollback provisions.

In 1995, CDI successfully obtained $9.8 million from the California State Legislature to prosecute insurers failing to pay their rebates. By the end of 1998, 157 rollback cases out of 169 had been successfully resolved.

CDI's aggressive efforts to implement Proposition 103 resulted in the approval of **472 rate decreases** between 1995-98 totaling $306 million in auto insurance premium savings for consumers in 1998 alone. Combined with the $466 million in premium rebates, California's consumers saved a total of $772 million. CDI's efforts to encourage lower insurance rates, and keeping them low, has paid off in consistently lower premiums for drivers. As *Exhibit 3* illustrates, the number of auto rate decreases approved by CDI was only 67 between 1991 and 1994, in contrast to the 472 rate decreases approved between 1995 and 1998.

***Exhibit 3: Personal Automobile Liability Insurance Rate Changes***

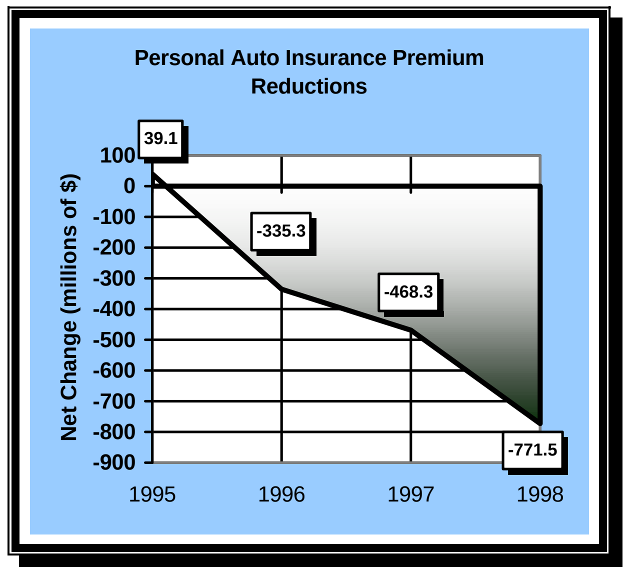



Source:Department of Insurance, Rate Regulation Branch, February 19, 1999.

CDI's Rate Regulation Division began tracking and verifying the impact of premiums under Proposition 103 regulations in early 1995 and found that the net savings to California's auto insurance consumers was approximately $1.5 billion between 1995 and 1998, as illustrated in *Exhibit 4*.

During the period from 1995 to 1998 auto insurance rates decreased significantly for California drivers. In fact, in 1998 the *Los Angeles Times*[7] described the market as being in an "auto insurance price war, which has already seen rates fall by an average of 5.5% in the last three years." In fact, rates dropped in some urban areas by as much as 17%. These rate reductions were a major component of the $772 million savings in premiums.

***Exhibit 4: Personal Automobile Insurance Premium Reductions***

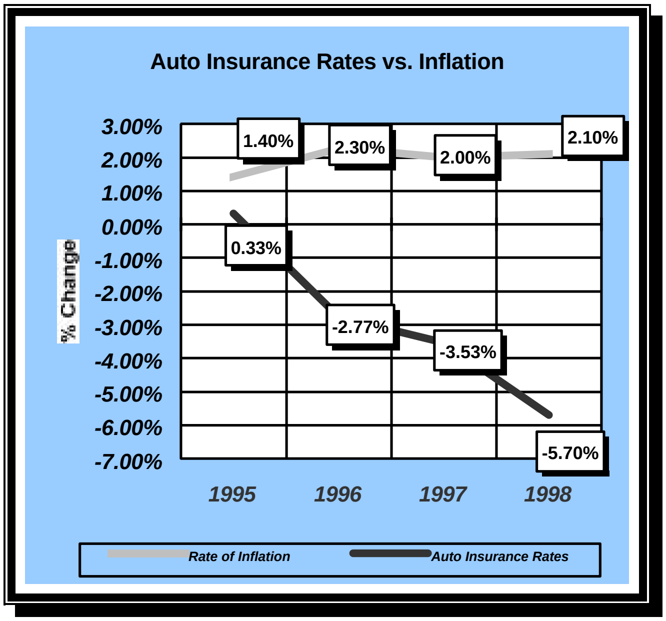



Source: CDI Rate Regulation Branch, February 19, 1999.
*Note:Premium impact information is not available for years 1991-1994.*

A comparison of auto insurance rates in California against the rate of inflation is another indicator of how much auto insurance rates in California have declined since 1995. As illustrated in *Exhibit 5*, auto insurance rates in California have steadily decreased since 1996 while inflation has increased at an annual average rate of nearly 2%. This data reflects real cost savings for California's drivers. As rates fell, many insurance companies advertised their rate reductions to attract new customers.

[7] *Los Angeles Times*, July 7, 1998.

*Exhibit 5:Automobile Insurance Rates Compared with Inflation, 95-98*




Source: CDI Rate Regulation Branch, March 1999.
*Note: 1998 figures are estimates as 1998 premium data.*

Observers have noted the tangible effects of the Department's aggressive implementation of Proposition 103 rate rollbacks. A spokeswoman from the *Proposition 103 Enforcement Project*, an issue advocacy group, stated in a *Los Angeles Times* article that consumers have "probably benefited overall." The benefits of CDI's regulatory approach have changed the dynamics of the auto insurance market over the last four years as noted by these commentators:

> *"Every major California insurer has cut its rates in the last year as new competitors enter the market."*
>
> – ***Los Angeles Times***, July 7, 1998[8]

> *"Auto insurance rates—which have a high profile in car-happy California—have dipped 5.5 percent since [Quackenbush] took office."*
>
> – ***San Jose Mercury News***, May 27, 1998[9]

> *"California's auto insurance business has become increasingly competitive, with companies cutting rates and improving services."*
>
> – ***Los Angeles Times***, July 19, 1998[10]

CDI has demonstrated that a regulator focused on encouraging effective market competition can be a catalyst for rate reductions.

## Driver Safety Record

Proposition 103 mandates that a person's Driving Safety Record (DSR), i.e. the number of points on a driver's record, be one of the primary factors in determining a driver's insurance rate. Implementing this requirement was difficult, requiring a significant change in the rating practices used by insurance companies.

CDI announced in October 1997 that the Department was implementing new permanent regulations that would de-emphasize zip codes as a factor in setting auto insurance premiums. The new rating formula requires insurance companies to appropriately weight a person's driving record, annual mileage driven and years of driving experience as principal criteria. CDI's new regulations also ensure that the state's lesser-populated areas are not subsidizing the more populated urban areas of California.

As a result, auto insurance companies in California now pay more attention to tickets and at-fault accidents when insuring drivers, complying with the letter and spirit of Proposition 103. The more DSR points drivers have on their records, the greater the chance their insurance rates will increase. Furthermore, recently adopted regulations allow for policies to be canceled or non-renewed if a driver gets three points or one major two-point violation, like a DUI, on their driving record within a 36-month period. This assures good drivers that they are not subsidizing other more accident-prone or careless drivers.

The core of Proposition 103 in regard to auto insurance is that it entitles insured drivers in California who have at least three years of driving experience (18 months of which must be in the U.S.) and no more than one point on their driving record to an insurance rate 20% lower than rates for drivers with two or more points.

## Automated Rate Comparison System

As of November 1994, CDI still had not addressed Proposition 103's requirement that CDI provide a comparison of the rate in effect for each personal line of insurance for every insurer. In fact, two previous insurance commissioners did not make such an automated rate comparison system available. In September 1998, nearly 10 years after Proposition 103's passage, CDI completed the implementation of this system and unveiled it to the public.

Today, California consumers can access comprehensive data on rates being offered by all companies providing auto and homeowner insurance in the state.[11] Armed with this information, consumers can be more informed about their insurance provider selection. Because consumers have

[8] *Los Angeles Times*, July 7, 1998
[9] *San Jose Mercury News*, May 27, 1998
[10] *Los Angeles Times*, July 10, 1998

[11] The Automated Rate Comparison System can be accessed at the California Department of Insurance's web site: *www.insurance.ca.gov.*

open access to this convenient source of comparative rate data, insurers also have an incentive to keep their rates as competitive as possible.

## Legislative Initiatives

CDI has worked diligently to save money for California's drivers by helping to enact key legislation, protect good, law-abiding drivers, and create new, tougher sentences on scam artists that commit staged auto collisions. In addition, Insurance Commissioner Chuck Quackenbush also sponsored a voter initiative to prevent drunk drivers and uninsured drivers from collecting pain and suffering damages after an auto accident.

### AB 650 (Chapter 1126/Sept. 1996) – Proof of Auto Insurance

CDI was one of the early supporters of AB 650 (Chapter 1126/Sept. 1996). This legislation requires drivers to show proof of insurance when renewing annual auto registrations with the Department of Motor Vehicles. Upon renewal of a vehicle registration, a driver must show proof of insurance or other compliance with the financial responsibility laws. Also, a driver must provide proof of insurance or financial responsibility to a peace officer at a traffic accident or if the driver is cited for a violation of the Vehicle Code.

Prior to this law, responsible, insured motorists were, in effect, subsidizing uninsured motorists by having to pay higher premiums that factored in the relatively high risk that they would be struck by an uninsured driver. By making insurance coverage mandatory for all vehicle owners, AB 650 was publicly acknowledged as a benefit to conscientious and responsible drivers and is one of the factors that has led to more insured drivers in California.

> *"The drop [in the number of uninsured drivers] has meant a boon to drivers: Car insurance rates have dipped 5.5 percent while rates nationally are rising."*[12]
>
> **– Los Angeles Daily News**

CDI's work in support of AB 650 has helped broaden the ranks of insured motorists, a key step toward an insurance system that is more fair and affordable for all drivers.

### SB 334 (Chapter 189/July 1998) – Fraudulent Auto Accidents

There are many forms of insurance fraud, but CDI places particular emphasis on an especially treacherous kind of auto fraud – staged auto collisions. Criminals who intentionally victimize innocent and unwitting motorists for the purpose of collecting insurance proceeds commit staged auto collisions.

To stage an accident, criminals swerve, or stop suddenly, in front of innocent drivers often causing a relatively minor collision, then demand money for their "injuries." Corrupt attorneys and doctors are often participants in organized fraud rings and act as collaborators in the crime by preparing fabricated and inflated injury reports.

One auto accident fraud scheme in Orange County involved 66 separate accidents or stolen vehicles, cost consumers in excess of $1 million in fraudulent auto insurance claims, and involved 24 insurance companies. It took two years of investigation by CDI and local law enforcement to break this crime ring and bring 86 suspects to arrest.[13] This type of insurance fraud is becoming more frequent and it increases the price of auto insurance for all insured drivers, but more importantly it risks the lives of innocent drivers, as was the case with the staged collision that took the lives of a young Long Beach family.[14]

SB 334 (Chapter 189/July 1998) was passed in 1998 to make staging an auto collision, for the purpose of fraudulently collecting insurance proceeds, a "serious felony" and subjects the suspect, if convicted, to the California "three strikes" law. Before SB 334 (Chapter 189/July 1998), a perpetrator of a staged auto collision faced a maximum two-year sentence and a $50,000 fine.

There is much more that needs to be done to stop staged auto collisions. As new legislation, such as SB 334 (Chapter 189/July 1998), is enacted to deter and punish criminals committing fraud, the sober task of protecting the innocent will continue. CDI places no higher premium on any of its responsibilities than protecting and defending consumers from abuse and fraud.

### Proposition 213 – The Personal Responsibility Act

In 1996, Commissioner Chuck Quackenbush authored and sponsored Proposition 213, the *Personal Responsibility Act.* This initiative prevents uninsured motorists and drunk drivers from collecting pain and suffering damages after an auto accident. It also bars compensation for any loss incurred by felons who were involved in automobile accidents while committing or fleeing from a crime. The proposition was approved by 77% of the voters—the highest percentage received by a ballot measure in over 60

[12] *Los Angeles Daily News*, August 4, 1998.

[13] California Department of Insurance Press Release #004, January 7, 1998.

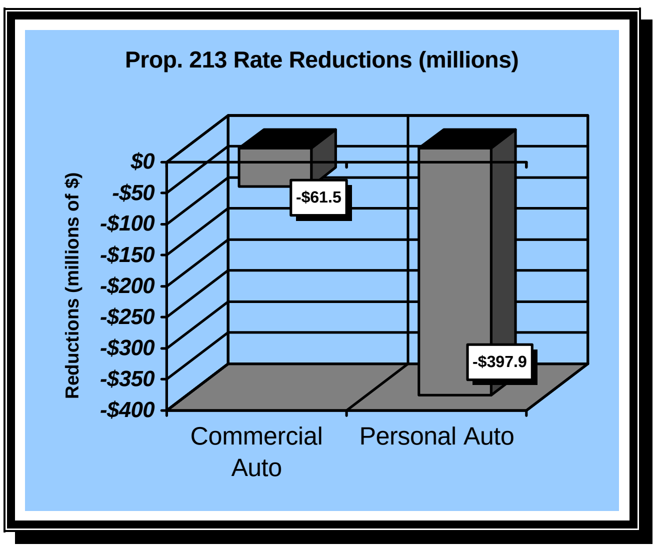
[14] California Department of Insurance Press Release #097, September 11, 1997.

years.[15] Since the passage of the Proposition 213, other states, such as Hawaii and New Jersey are adopting similar versions of the initiative's "no pay, no play" policy provisions.

Since Proposition 213 dramatically reduced liability exposure, CDI required California's automobile insurers to submit rate reduction filings reflecting anticipated savings. In total, CDI received 572 filings, representing a 9.49% decline in automobile liability coverage rates and resulting in savings amounting to nearly $460 million. *Exhibit 6* summarizes the generated savings of these rate reductions for California's drivers.

The period of 1995 to 1998 can only be characterized as phenomenal. The savings generated by the reduction of liability exposure from Proposition 213, combined with the rebate and rollback savings from Proposition 103, means that **California's consumers have saved over $1.5 billion** in auto insurance premium reductions during the last four years.

***Exhibit 6:Insurance Rate Reductions from Proposition 213***




Source: Proposition 213 Summary Report, CDI Regulation Branch.

## *Innovative Automobile "Mini-Policy"*

California law now requires drivers to be financially responsible and protect other persons for any damage that they may cause. However, an estimated 22% of California motorists presently drive without auto insurance.[16] Affordability is often an issue for many low-to-moderate income drivers who may not be able to afford the cost of standard conventional automobile insurance coverage. In 1998, CDI developed an innovative new type of auto insurance policy, called the "Auto Mini Policy" as a low-cost alternative to standard conventional auto insurance.

A standard auto insurance policy provides features or coverage that may not be needed by all drivers. The "mini policy" provides an alternative by scaling the standard policy down to a few core essential elements of coverage, thus creating a minimum policy, or "mini policy," without all the features and coverage typically included in a standard policy.

The "mini policy" contains the following requirements:

***First***, the "mini policy" provides consumers with a reasonable insurance premium in exchange for a consumer's assurance not to engage in risky behavior, such as drinking and driving. Failure to adhere to these pledges would result in higher out-of-pocket costs in the form of a higher deductible, but still provide adequate protection for other drivers.

***Second***, the "mini policy" would not cover "permissive drivers" (i.e. drivers permitted to drive the insured's vehicle, although not expressly named in the policy). Currently, there is a requirement in law that all auto insurance policies must cover permissive users; consequently premiums for all drivers are higher. Using a "mini policy" that does not cover permissive users will reduce the cost of liability premiums while still ensuring that people have insurance to get to and from work and take care of day-to-day errands, such as grocery shopping. At their option, consumers would be able to add on a permissive-user endorsement for an extra premium, if they wanted or needed this coverage.

Providing a low-cost choice for consumers would provide an important option for cost-conscious insureds. And, offering alternatives to the standard policy may eventually lead to lower premiums for all drivers.

This initiative dovetails with many of CDI's goals, namely to serve low to moderate-income communities and to further encourage reduced-cost automobile insurance. If implemented, CDI estimates that drivers with an auto "mini policy" would enjoy premium savings of up to 15% as compared to those with a standard policy.

All the provisions required of a standard automobile liability policy, with their resulting costs, may not meet the needs of all persons, particularly those who rely on their car to get to and from work. Removing the requirement for coverage of permissive drivers would result in a lower cost policy and make insurance more affordable to those who currently do not purchase coverage because of cost considerations.

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[15] California Department of Insurance, speech before the Conference on Insurance Regulation: *California: the Insurance Forefront*, July 9, 1998.
[16] California Department of Insurance, *Low Cost Auto Insurance: Named Driver Only Policy*, undated document.

# EXPANDED ACCESS TO INSURANCE INFORMATION

CDI understands that Californians expect an insurance regulator to protect consumers. CDI believes that a key aspect of this protection involves providing assistance to consumers in finding the best insurance value and helping them to understand their rights as insurance consumers. That is why CDI's highest priority is protecting California's consumers and maximizing the powerful benefits of free-market principles.

CDI recognizes that imperfect or incomplete consumer information and unequal bargaining power between insurers and consumers can make consumers vulnerable to abusive marketing and claims practices of insurers and producers. Enhancing consumer information about insurers' financial strength, products, and prices is critical to ensure competition and good market performance. CDI is a leader in providing consumers with access to information they can use to make rational decisions among the often mind-boggling alternatives available in the insurance market. Using advanced information technology tools, such as the Internet, and other communication channels, CDI has helped make Californians more knowledgeable and better insurance consumers.

## *Award-Winning CDI Web Site*

The CDI Internet web site has received national recognition for providing consumers with comprehensive information about the insurance industry. The web page offers important information for California consumers, insurance producers and insurance carriers, including:

- Premium rates comparisons for automobile, homeowner, rental, condominium, earthquake, and title insurance.
- CDI's *Request for Assistance* forms for use in filing grievances against insurers.
- Comparative information on complaints against insurers.
- Information on fraudulent insurance activities.
- Instant agent license check, providing status, history and any disciplinary actions.
- Consumer brochures with helpful information on a wide variety of subjects related to insurance.

An *Internet Advisory Committee* made up of CDI employees throughout the Department, including the Consumer Ombudsman, administers CDI's Web site. These content developers are responsible for creating helpful, informative, and interesting features of the web site. *Exhibit 7* outlines the extensive information and resources available at the CDI Web site located at *www.insurance.ca.gov*.

***Exhibit 7: California Department of Insurance Web Site Information***

**Looking for Insurance?**

- Check to See if your Agent or Broker is Licensed
- Premium Comparisons
- General Insurance Information
- Consumer Complaint Study
- *Consumer Alert*
- Insurance Company Profiles
- Need Help Finding an Agent?

**Having Problems with Your Insurance?**

- Disaster Assistance
- Catastrophe Series
- Claim Tips
- How to File a Complaint
- Unpaid Holocaust Claims
- Proposition 103 Rebate Status

**Who's Looking Out for Your Interests?**

- Consumer Services
- CDI Policy Initiatives
- Boards, Advisory Committees and Commissions
- Intervenor Program

**Fighting Insurance Fraud**

- *Most Wanted*
- *Undercover*
- Auto Insurance Fraud
- Workers' Compensation Fraud
- Special Operations
- History of Fighting Fraud

**Financial Oversight**

- Company Financial Reports
- Court-approved Sale of an Insurance Company
- Year 2000 Compliance Project

**Legal Materials & Information**

- Precedential Decisions of the Commissioner
- Research Studies and Auto Class Plan Information
- CEA Rate Hearing
- Regulations
- Insurance Code

Source: California Department of Insurance, Office of the Ombudsman, 1998

Since the web site's launch, activity has grown to over 500,000 "hits" every month and continues to climb.[17] The site's most popular features include premium comparisons, agent and broker license information, enforcement actions, list of admitted companies, Fraud Branch's Most Wanted list, and consumer complaint studies. In addition to the regular favorites, CDI's Web site includes seasonal features such as pertinent information about various types of natural disasters common to California. This feature is updated every few months to provide information about seasonal topics such as increased fire danger in the summer, flooding in the spring, and mudslides in the winter.

The CDI Web site has garnered numerous awards for the comprehensive content of information for insurance consumers and its quality presentation. In fact, CDI's Web site is a model used by the National Association of Insurance Commissioners (NAIC) and CDI staff co-authored the NAIC's *White Paper on the Internet*[18] that explores the unique possibilities of using the Internet in insurance regulation.

## *Consumer Outreach*

Information is essential and it is CDI's obligation to make sure that the public is adequately informed. CDI is committed to proactively providing consumers with practical and timely information about the insurance industry and CDI's *Outreach Program* serves that objective.

To further outreach efforts, CDI expanded distribution of consumer information and education by publishing brochures, speaking at schools and community groups, attending town-hall meetings and other forums. CDI's *Outreach Program* participated in 159 events between 1995-1999. In addition, CDI's Fraud Branch conducted 862 training and public presentations between July and December 1998.[19]

### Public Service Announcements

On December 2, 1997, CDI announced a major outreach program designed to increase public awareness about millions of unclaimed dollars that might be owed to consumers from Proposition 103 auto insurance rebates, enforcement actions, liquidated assets, class-action settlements, and restitution awards.[20] CDI aired 30-second public service announcements on television and radio across California to inform consumers on how consumers can easily determine if money is owed to them and how to file a claim.

CDI also announced on August 25, 1998, that the Department would begin a major consumer outreach program designed to increase consumer awareness about money that may be owed on unpaid Holocaust-era insurance claims.

### Insurance Information Published in Several Languages

CDI sought not only to increase the amount of quality information available, but also sponsored legislation[21] in 1995 to enable the CDI to produce consumer information booklets in commonly spoken **non-English** languages – particularly Spanish and Vietnamese. As a result, CDI began publishing Spanish and Vietnamese versions of the Department's brochures in 1997 in addition to the English versions. Approximately 6,000 brochures are distributed each month in English, Spanish and Vietnamese translations.[22]

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[17] California Department of Insurance, Office of the Ombudsman,.
[18] National Association of Insurance Commissioners, *White Paper on the Internet*, March 16, 1998,
[19] California Department of Insurance, Press Office, Consumer Outreach Overview, memorandum dated March 19, 1999.
[20] California Department of Insurance, Press Office, Consumer Outreach Overview, memorandum dated March 19, 1999.
[21] AB 1150 Chapter 909/Oct. 1995)
[22] California Department of Insurance, Press Office, Consumer Outreach Overview, memorandum dated March 19, 1999.

# IMPROVED INSURANCE MARKET

The availability and cost of insurance coverage affect virtually all California consumers. A prime example is that no lender will make a home loan without homeowner's insurance. The average consumer typically expects insurance premiums to steadily rise, as is often the trend of most products we purchase. However, a top CDI priority has been to reverse this trend of ever-increasing premiums by stimulating competition in the California insurance marketplace and, where necessary, offer regulatory assistance to bolster deficient insurance markets.

## *Restored Stability in the Homeowner's Insurance Market*

CDI's response to past failing homeowner's and earthquake insurance markets demonstrates that a regulator can provide effective solutions when the private sector is unable to do so. After the 1994 Northridge earthquake capsized the homeowner's and earthquake insurance markets, CDI stepped in with innovative proposals – most notably, the creation of the *California Earthquake Authority* – to stabilize those markets. CDI's innovation and leadership helped to ensure that tens of thousands of Californians were once again able to obtain homeowner's and earthquake insurance policies in the wake of the crisis.

### Stabilized the Earthquake Insurance Market

The "American dream" of home ownership turned into a nightmare for many Californians during the mid-1990's. A string of major earthquakes, most notably the Northridge earthquake in 1994, sent shock waves through companies that provide homeowner's insurance. Insurers, suddenly facing billions of dollars in claims, became wary of writing new policies, especially since California law mandates that insurers offering homeowner's policies are required to offer residential earthquake coverage with no underwriting restrictions.[23] This mandate made homeowner's policies too costly to underwrite and insurers, in turn, began drastically reducing the number of new homeowner's insurance policies. But, the insurers' shyness from the homeowner's market did not stop there. Insuring the high-risk, earthquake-prone regions of the Los Angeles Basin and the San Francisco Bay Area placed such an excessive financial liability on insurers that they were unable to renew many existing customer's policies, leaving a rapidly increasing number of homeowners without any protection from risk. At the height of the crisis in the summer of 1996, 95% of the homeowner's market had either stopped completely or severely restricted the writing of new homeowners insurance.[24]

Although insurers could not refuse to provide unrestricted earthquake coverage, they could establish more restrictive qualifying underwriting requirements on homeowner's and dwelling fire insurance for new business and renewals. Additionally, they could limit the number of new homeowner and dwelling fire policies written.[25]

As a result, most insurers who wrote residential property insurance in California either placed more restrictive qualifying underwriting requirements on their homeowner and dwelling fire business and/or they limited the number of policies and amount of business written. Underwriting restrictions included such criteria as:[26]

- Homes could not be within *x* number of miles of an earthquake fault line.
- A home's dwelling value could not exceeded *x* amount of dollars.
- No coverage for homes made of brick or masonry construction.
- No coverage for dwellings with open foundations.
- No coverage for dwellings built on hillsides or slopes exceeding *x* degrees.
- No coverage for homes exceeding two stories in height.
- No coverage for homes built prior to 1950, unless they had been retrofitted.
- No concentration of multiple dwellings within a specified geographic area.
- No coverage for homes in areas with limited accessibility.

These restrictions or limitations created a severe shortage of coverage availability in the residential dwelling marketplace. CDI took several significant steps to re-establish the availability and affordability of homeowner insurance for

[23] California Insurance Code Section 10081

[24] SB 395 (Chapter 899/Oct. 1995)

[25] California Department of Insurance, Rate Regulation Branch, memorandum dated March 22, 1999.

[26] California Department of Insurance, Rate Regulation Branch, memorandum dated March 22, 1999.

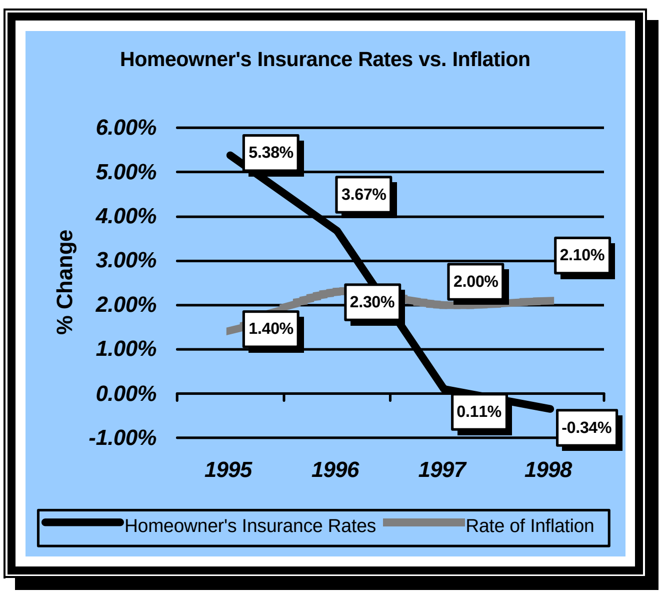
California's consumers. For example, CDI began working with insurance companies to encourage them to remove these restrictions from homeowner insurance policies and write homeowner's policies without restrictions.

Since 1995, the number of insurance companies writing homeowner's insurance with restrictions dropped from a high of 82 in July 1996 to a low of three in October 1997. During this same period, the number of companies writing without restrictions increased from a low of four companies to 107 companies.

In a significant trend reversal, the number of complaints from homeowners who could not find homeowner's insurance dropped from 3,000 calls per month to less than 200 calls per month at the end of 1998, a 1500% decrease.[27] This remarkable turnaround in the availability of homeowner's insurance ensures that home-buyers can close escrow and professionals such as realtors, mortgage bankers, and the construction industry can continue to provide sound economic growth.

CDI not only helped make homeowner insurance more available, the Department also addressed the serious concern that homeowner insurance had become unaffordable. During the period of 1995 to 1998, rising homeowner's insurance premiums slowed and dropped to less than the rate of inflation. *Exhibit 8* contains an analysis of homeowner's insurance rates compared to inflation.

***Exhibit 8: Homeowner's Insurance Rates Compared vs. Inflation, 95–98***




Source: CDI Rate Regulation Branch, March 1999.
*Note: 1998 figures are estimates as 1998 premium data.*

In 1998, CDI began providing consumers with the ability to conduct comparative shopping for homeowner's insurance either by calling CDI's Consumer Hotline or accessing the information directly through CDI's Web Site.

## *The Cutting Edge - California Earthquake Authority*

The successful rehabilitation of the homeowner's insurance market was due, in large part, to the CDI's efforts to restore the integrity of the earthquake insurance marketplace. Restoring the earthquake insurance market was not only a vital part of protecting Californians in earthquake-prone areas; it was essential to restoring the homeowner's insurance market as a whole.

In July 1995, CDI proposed the formation of the California Earthquake Authority (CEA), a multi-billion dollar, government administered, but privately funded earthquake insurance pool. The concept was unique; in addition to the revenue collected on limited coverage earthquake policies, the CEA would pool funding from participating insurers, reinsurance, and other forms of financial commitments for the expressed purpose of protecting California's homeowners from the risk of earthquakes.

The story is one of remarkable success. By October 1, 1997, the CEA had the capacity to handle earthquake claims totaling approximately $6.9 billion. To put this capacity in perspective, if a Northridge-type earthquake were to have occurred on October 1, 1997 the estimated loss to the CEA would have been approximately $1.1 billion *(see Exhibit 9)*.

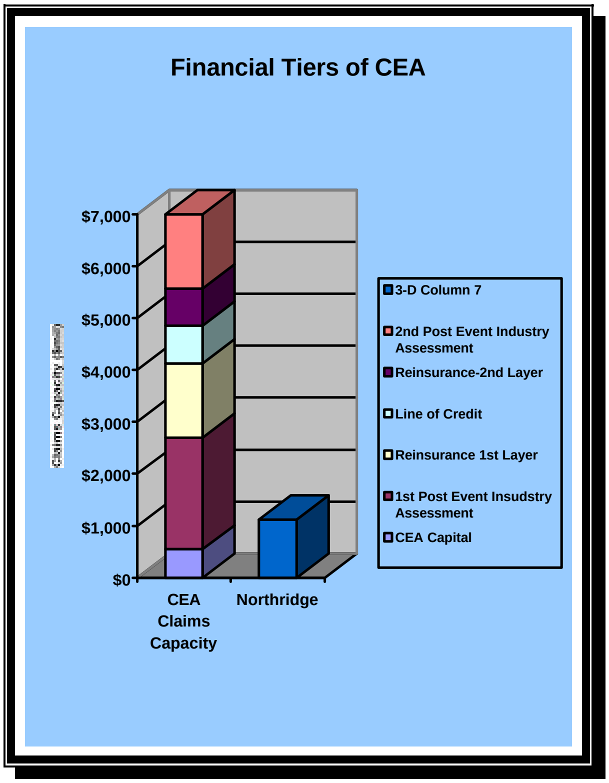
The CEA is now the largest earthquake insurer in the state, making earthquake insurance available for over 700,000 policyholders. The CEA is also required to take <u>all</u> applicants seeking earthquake insurance, thus eliminating a consumers' inability to purchase earthquake coverage.

Since the inception of the CEA, improved science and earthquake forecasting tools have led to better earthquake rating methodologies. During the CEA's first year of existence, CDI became aware of premium overcharges that averaged 11% statewide. In May 1998, CDI announced an 11% rate reduction had been approved that prompted refunds for CEA policyholders that resulted in total savings of $37.5 million for 650,000 California homeowners.[28]

[27] California Department of Insurance, Consumer Services and Market Conduct Branch, 1998.

[28] California Department of Insurance Press Release, #172, for release December 4, 1998.

***Exhibit 9: Financial Tiers of CEA***




Source: CEA (As of 10/1/1997)

In December 1998, CDI approved an additional 4.5% rate reduction filing submitted by the CEA.[29] This rate reduction was the result of the CEA's most recent scientific study and actuarial review of earthquake coverage that led to the development of further refined rating factors and adjustments to the CEA's rate setting methodologies. CDI has encouraged the CEA to continue in its efforts to make rate setting as scientifically based and financially sound as possible, thereby ensuring that the CEA's current 700,000-plus policyholders receive the best value and service possible.

## Earthquake Wrap-Around Policies

Following enactment of the CEA, CDI has worked to approve private sector insurers to offer supplementary earthquake coverage. So far, CDI has licensed two stand-alone private earthquake insurers to offer consumers more coverage than the single policy available from the CEA. These companies offer lower deductibles and expanded coverage over the CEA's policy and consumers can choose to supplement the CEA with coverage from these companies.

## Earthquake Grants and Loans Program

In the interest of earthquake prevention, CDI has initiated an *Earthquake Grants and Loans Program* for low and moderate-income homeowners to retrofit their homes and make them safer in the event of an earthquake. The program was piloted successfully in Los Angeles, Humboldt, and Alameda counties and has been expanded to San Francisco, Santa Cruz, San Bernardino, Mendocino, and San Diego counties. The low-interest loans and grant funds can be used for a variety of earthquake retrofit projects, including:

- Bolting homes to their foundations.
- Strengthening cripple walls.
- Anchoring hot water heaters.
- Installing automatic gas shut-off valves.
- Installing earthquake resistant bracing systems for mobile homes.

The existence of preventive programs, such as the *Earthquake Grants and Loans Program*, benefits insurance rates in California by reducing the number of claims and the severity of claims and ultimately leading to a reduction in rates.

## Earthquake Claims Mediation Program

CDI also instituted the *California Earthquake Claims Mediation Program* to provide a neutral forum for insurers and insureds to resolve disputed claims. Under the program, both parties voluntarily enter into the mediation program. After only six months in operation, the mediation program enabled consumers to receive nearly $7 million in claims payments that were disputed.[30]

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[29] California Department of Insurance Press Release #182, for release December 17, 1998.

[30] California Department of Insurance, Consumer Services Division and Market Conduct Branch, May 26, 1999.

## *Broadened Access to Health Insurance*

The availability of health care insurance is a major concern of many Californians. In January 1995, CDI went to work to help small business owners and their employees obtain inexpensive health care coverage and make that coverage more portable. CDI is also helping seniors obtain long-term care insurance coverage.

### Small Business COBRA's

CDI sponsored AB 2659 (1998), legislation to extend protection from the Consolidated Omnibus Reconciliation Act (COBRA) to employees of companies with two to 19 employees. This law allows employees of these small businesses to have the same health care protections as employees in larger companies. Such protection provides employees in nearly all California businesses with the security of being able to continue their group health insurance policy for up to 18 months while transitioning to another employer's health plan.

### Advocating Multiple, Competing HIPC's

CDI continues to seek legislation to allow private sector competition with the state's Health Insurance Plan of California (HIPC). Under current law, the HIPC allows the state's small business employers to join together to negotiate for better health insurance premiums with insurers and HMO's. Like a number of other states, California had enacted legislation creating health care purchasing alliances to benefit small businesses.

CDI is seeking to allow private entities to perform the same function as the state HIPC, which would increase the bargaining power of small employers and ultimately enable more employers to provide quality health insurance coverage for their employees. While these legislative efforts have not yet been successful, CDI will continue to explore alternatives that empower small employers to negotiate better health insurance premiums.

### Created Tax-Qualified Long-term care Policies in California

CDI worked to ensure that seniors had more opportunity to obtain long-term care insurance. Two years ago, the United States Congress authorized the sale of long-term care policies offering significant tax benefits. In 1997, CDI worked with the California State Legislature to modify California law to comply with Federal law and allow the sale of these tax-qualified products while ensuring that consumers still had the option to purchase non-tax-qualified products if they choose.

CDI has processed and approved long-term care filings from over a dozen long-term care insurers and now seniors have more choices for this type of insurance than ever before. CDI has made long-term care policy review a top priority of the Department's *Policy Approval Bureau* and CDI is strongly committed to increasing the availability and affordability of these new policies in the marketplace. As of February 23, 1999, CDI had received 327 filings from 49 companies, and 203 policies have been approved.[31]

### Reducing Consumers' Dependence on "Insurers of Last Resort"

One of CDI's major achievements has been curbing the withdrawal of admitted insurers from the California insurance market, which was forcing a substantial number of consumers into state residual markets.

When the insurance market is functioning properly, admitted insurers licensed by CDI provide coverage for most consumers. Because of problems with restrictive price regulation, affordability and capacity, however, admitted insurers might not always meet the demand for essential insurance products. The hope is that problems in the marketplace only exist temporarily and should disappear when market conditions change and improve. But, at those times when admitted insurers are not able to fulfill the demand, a residual market, often referred to as an "insurer of last resort" is established to satisfy the consumer's demand for essential insurance coverage.[32]

Usually a residual market is established for insurance coverage that is mandated by law, such as automobile liability coverage or workers' compensation insurance. Residual markets may also be created to provide consumers with insurance that are not state-mandated, but may be necessary for business transactions. For instance, lenders may require borrowers to obtain property insurance for vehicles or buildings and personal property to protect the creditor's collateral. In brief, a residual market is where you might have to turn if you cannot obtain the necessary insurance in other ways.

Although residual markets are a common mechanism to compensate for insufficient market competition, CDI has attempted to reduce consumers' dependence on the residual market. Efforts to encourage private insurers to compete for business in California has resulted in fewer individuals who are forced to rely on two of California's largest residual market programs: the **California Automobile Assigned Risk Plan** (CAARP) for auto insurance, and the **Fair Access to Insurance Requirements** (FAIR) Plan for urban risks and brush fire areas.

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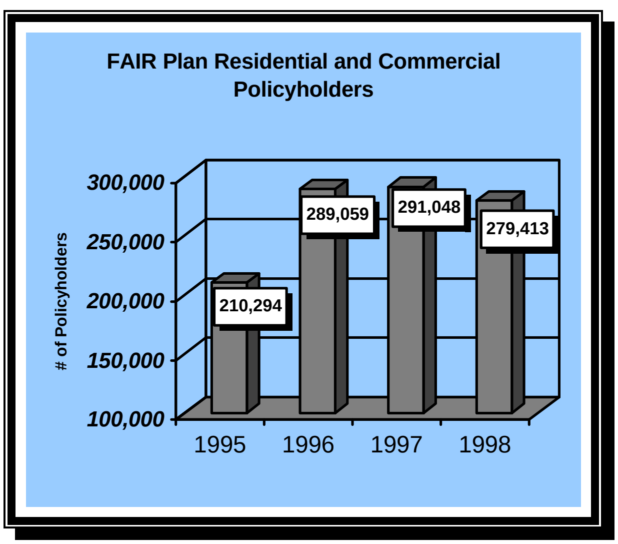
[31] California Department of Insurance, Rate Regulation Branch,1998.
[32] Insurance Institute of America, *Surplus Lines Insurance Principles and Issues, 2nd Edition*, William R. Feldhaus, PhD, Coordinating Editor, and Doris Hoops, Coordinating Author, July 1997, page 61.

## The FAIR Plan

The **California Fair Access to Insurance Requirements (FAIR) Plan Association** was created by statute in 1968 as an outgrowth of the 1961 Bel Air Canyon fires and the 1965 Watts riots.[33] At that time, there were concerns across the country that, because of the nature of risks inherent with the inner cities, persons living and operating businesses in urban areas would have difficulty obtaining insurance. Since 1968, the FAIR Plan has not only served as the "insurer of last resort" for urban risks, but also for areas prone to brush fire, because of the high risk and prevalence in California.[34] Programs similar to the FAIR Plan also exist in 29 other states and the District of Columbia to ensure that basic fire and, in some cases, extended coverage is available to property owners in urban areas.[35]

At the beginning of 1995, the number of policyholders in the FAIR Plan was climbing due to the crisis in homeowner insurance. CDI's efforts to resolve the homeowner crisis has resulted in a slight decrease in the number of participants in the FAIR Plan in 1998, as *Exhibit 10* indicates. According to the plan's Public Affairs Office, numbers for 1999 are expected to show a much more significant decline because the FAIR Plan is currently experiencing 1,100 per month net decline in the number of policyholders. The decrease in the number of FAIR Plan policyholders suggest that the private market is doing a better job of providing basic property insurance to urban areas, thus reducing dependence on the state's "insurer of last resort."

***Exhibit 10: FAIR Plan Residential and Commercial Policyholders, 95-98***

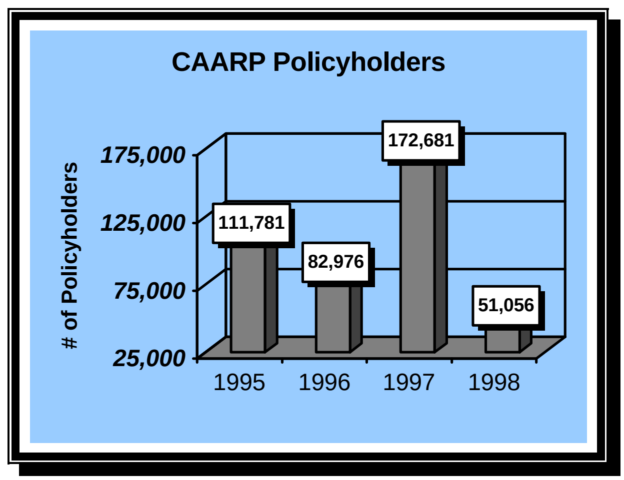



Source: California FAIR Plan Association, Public Affairs Office, April 15, 1999.

## The California Automobile Assigned Risk Plan

The **California Automobile Assigned Risk Plan** (CAARP) was created in 1947 after a law was passed requiring all persons to provide proof of financial responsibility prior to obtaining a driver's license. As a consequence, a large number of "poor risk" drivers were unable to receive licenses to drive because insurers were not willing to assume the higher risks.[36] Over 50 years later, CAARP still serves as the "insurer of last resort" for many Californians who are unable to obtain auto insurance in the private market. However, much improved and competitive market conditions are beginning to significantly decrease the number of California's consumers who cannot find affordable auto insurance from private insurers. *Exhibit 11* illustrates a substantial decline between 1995 and 1998 in CAARP policyholders, from 111,781 individuals in 1995 to 51,056 in 1998.

***Exhibit 11: CAARP Policyholders, 95-98***




Source: California Automobile Assigned Risk Plan, April 13, 1999.
*Note: Statistics reflect private passenger non-fleet applications assigned.*

The noticeable spike in the number of participants in 1997 can be attributed to the passage of AB 650, requiring drivers to carry proof of auto insurance. However, the private insurance market has been aggressively competing for business resulting in fewer policies written through CAARP. Additionally, insurers' private passenger auto liability rates have gone consistently down, making insurance generally more affordable for all consumers and lessening consumer dependence on this residual market.

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[33] California FAIR Plan Association, Public Affairs Office, April 15, 1999. The California FAIR Plan was created after the passage of the 1968 Federal Riot and Reinsurance Act.
[34] California Department of Insurance, memorandum dated April 14, 1999.
[35] *Surplus Lines Insurance Principles and Issues*, page. 61.

[36] California Department of Insurance, California Automobile Assigned Risk Plan Representative, April 13, 1999. See also *CSAA v. Maloney*, 71 S.Ct. 601, 602 (1951).

# AGGRESSIVE ENFORCEMENT ACTIONS

Over the last four years, CDI has led an unprecedented effort to punish illegal and abusive insurance practices by insurance providers. Consumers depend upon CDI to enforce the laws and provide consumer protection regarding insurance claims paying, rating, and underwriting. In essence, consumers need a properly monitored marketplace that ensures fair treatment. CDI believes that taking quick and decisive action against "bad" actors in the industry is the most effective strategy for cleaning up the insurance marketplace and preserving the integrity of the industry to make it beneficial for all.

This vision has led the Department to dramatically increase its enforcement activities against insurance carriers and producers over previous years in both volume of cases and dollar amounts recovered for policyholders.

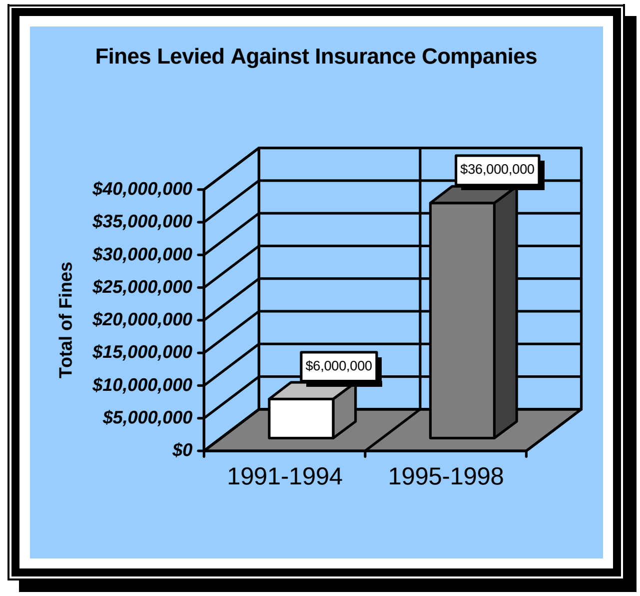
## *Protecting California's Consumers*

CDI protects California policyholders by closely monitoring the insurance industry for improper and fraudulent claims resolution practices. From 1995 to 1998, CDI completed disciplinary actions against 62 insurance companies and levied over $36 million in fines – *a record for CDI*.[37] Notable actions by CDI's Enforcement Branch include:

- A $15.4 million penalty against an insurance company for deceptive sales practices possibly affecting hundreds of thousands of company policyholders in California.
- Multi-jurisdictional enforcement action against an insurance company for deceptive practices against its customers in the sale of credit insurance.
- Extensive restitution / remediation for injured policyholders in actions brought against three insurance companies.[38]

To put the significance of these fines in perspective, during 1991 to 1994, the previous administration levied only $6 million in fines.

*Exhibit 12: Fines Against Insurance Companies, 1991-94 vs. 1995-98*




Source: California Department of Insurance, 1999.

## Investigative Activities

CDI participated in a multi-state investigation into allegations that the company's sales agents engaged in improper sales tactics commonly known as "churning." Evidence uncovered by investigators revealed that thousands of policyholders in California were persuaded by a company's agents to exchange the cash value of their existing life insurance policies for higher value policies. Customers relied on representations by the company that the cash values of the existing policies were adequate to finance the larger policies at no additional cost. Many Californians were shocked when premium notices subsequently arrived in the mail. Some victims lost their life insurance policies altogether when they could not afford the higher premiums. Senior citizens, who had accumulated high cash values by paying premiums for many years, were disproportionately victimized by these improper practices.[39]

On February 21, 1997, CDI announced a record $15.4 million fine against the company– the largest single fine in CDI history. As part of this enforcement action, CDI

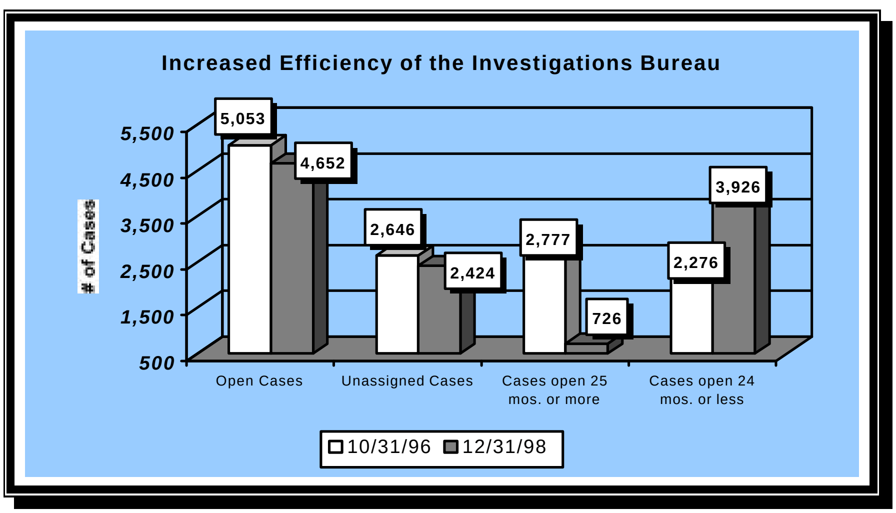
[37] California Department of Insurance, Enforcement Branch, 1998.
[38] California Department of Insurance, Enforcement Branch, 1998.
[39] Letter from Commissioner Chuck Quackenbush to the Honorable Liz Figueroa, Chair, Assembly Committee on Insurance, dated May 23, 1997.

ordered a significant portion of the settlement to be allocated to contacting the company's approximately 625,000 policyholders in California and inform them of their right to pursue relief under a court-appointed remediation program.[40] By May 12, 1997, the CDI Hotline was receiving an average of 1,800 calls per week from consumers affected by a particular insurance company.[41] As a result of this outreach program, over 180,000 Californians, or approximately 26% of the eligible company policyholders in the state, applied for relief. This level of participation by consumers was 72% higher than the national response rate to similar actions taken in other states.[42]

## Efficiency and Effectiveness

Part of the reason why the amount of fines paid by insurers perpetrating illegal activities has increased in recent years is because the CDI has increased the efficiency and effectiveness of its complaint investigations process. As demonstrated in *Exhibit 13*, the CDI's ability to enforce insurance regulations has been significantly enhanced. The process has been streamlined so investigators can resolve cases more quickly, and thereby handle a greater volume of cases. For instance, the number of cases open 25 months or greater has declined by 70%. High priority cases are also being resolved more quickly; 54% of all "Priority 1" cases are resolved within 12 months.

***Exhibit 13: Indicators of Investigations Bureau's Increased Efficiency***




Source: California Department of Insurance, 1999.

## Enacted Consumer Protections to Reduce Illegal Activities by Agents and Brokers

The Department takes its obligation to protect consumers from abusive tactics by insurance providers very seriously. For example, *Eastwood Insurance Services*, a large insurance agency, was fined $300,000 for transacting insurance through unlicensed persons and acting as an insurance agent for an unlicensed insurer.[43] Without proper agent licensure, consumers do not have the assurance that they are buying insurance from a competent agent.

An important component of the Department's enforcement policies is its stand against insurance agents and brokers who violate insurance statutes and fair business practices. CDI has completed disciplinary actions against 1,828 insurance agents and brokers, including the revocation of 901 licenses and denial of 252 licenses to "bad actors."[44] In addition, CDI has sponsored legislation to better protect California consumers against potential abuses by insurance agents and brokers, including:

- Legislation to expand Commissioner's cease and desist authority to stop illegal activities.
- Legislation to expand the power of summary revocation for agents and brokers who have pleaded guilty, or *nolo contendere*, for crimes relating to the business of insurance.
- Legislation to require the licensure of car rental firms and credit insurance sellers to bring those insurance sales-related activities under regulatory oversight and safeguards.
- Budget augmentation to add 25 employees for FY 1999-2000 to investigate producer misconduct. Adding these 25 employees will greatly assist in eliminating the investigations backlog.[45]

In addition to legislative attempts, CDI has implemented new initiatives to better educate and protect consumers against potential insurance agent or broker abuse, including:

- Creating *Consumer Alert*, an interactive agent/broker licensing database on the CDI Web site.

[40] California Department of Insurance, Enforcement Division, *Enforcement Accomplishments, 1995-1998*, March 1999
[41] California Department of Insurance, Consumer Services and Market Conduct Branch, 1998.
[42] California Department of Insurance, Memorandum dated March 19, 1999.
[43] California Department of Insurance, 1998.
[44] California Department of Insurance, Enforcement Division, *Enforcement Accomplishments, 1995-1998*, March 1999.
[45] Department of Finance Memoranda, 1999.

- Direct mail and media outreach to potential victims to inform them of relief to which they may be entitled.
- Proposed new regulations that will require brokers to provide prospective auto and homeowner clients with CDI's consumer information brochure on buying auto and homeowner insurance.

## Enhanced Investigation Capabilities

By the end of 1996, CDI staff had reduced the backlog of 6,500 open cases involving agents and brokers by 25%. CDI has actively sought additional investigators to ensure that all investigations of insurance agents and brokers are completed efficiently.[46] CDI has also successfully sponsored legislation to obtain limited police powers for these investigators and assist them in cracking down on criminal activity.

Also, CDI is attempting to put an end to the practice of fiscal considerations adversely influencing the priorities and decisions surrounding investigations. Because of past budget impediments, the Department has been compelled to focus on performing only those investigations for which it could be reimbursed. This method has led to awkward and often detrimental choices about whether to investigate high-priority non-reimbursable cases or low-priority reimbursable cases.

CDI considers this practice inconsistent with the Commissioner's vision statement. Consumers deserve to have adequate protection against abusive practices and CDI has fought vigorously to obtain the necessary resources to allow investigators to assume the most important cases, regardless of whether the target has assets to pay for the investigation. For the first time in the Department's history, the 1998-1999 state budget included adequate resources to allow Department investigators to focus on consumer protection, instead of budgetary considerations.

## Supervise Sales and Underwriting Activities

As California's insurance regulator, CDI closely monitors the sales and underwriting practices of insurers and producers to make sure they adhere to legal and ethical standards, and that claims are handled fairly and according to the provisions of the insurance contract. The objective is to prevent abusive practices that take unfair advantage of consumers; i.e., false sales illustrations or failure to pay legitimate claims on a timely basis. Responding to consumer complaints and performing market conduct examinations are the primary methods by which CDI regulates market practices.

[46] Senate Insurance Committee Hearing—February 25, 1999, Department of Insurance Responses to Information Requests, p. 3.

Market conduct examinations are conducted on a routine basis, but can also be triggered by consumer complaints. During a market conduct examination, examiners review a random sampling of a company's policy files and claims files as well as other internal records to ensure that the company is acting in compliance with state laws and regulations. Generally, examiners check to see that the rates charged are consistent with the rates that are filed and approved by CDI, and that claims covered under a policy are paid within a reasonable period of time.

Unfortunately, during 1997 and 1998 both the *Field Rating and Underwriting Bureau* and the *Market Conduct Bureau* suffered major staff reductions. As a result, the number of examinations filed and amount of premiums recovered by the *Field Rating and Underwriting Bureau* decreased; in 1996, 118 examinations were filed and $2.7 million in premiums recovered. In contrast, only 82 examinations were filed and $1.2 million recovered in 1997-98.[47]

Similarly, the effectiveness of the *Market Conduct Bureau* decreased due to staff reductions; in 1996, 48 claims were filed and claim recoveries amounted to $1.2 million, but by 1998 the amount of claim recoveries was only $160,390.[48] However, both bureaus recently adopted revised examination procedures that will allow them to greatly increase examination efficiency.

With a focus on personal lines, small business policies, and third party claims activities, both bureaus play a critical role in the oversight and regulation of insurer rating, underwriting, and claims-handling practices.

## *"Consumer Alert"*

Each month, CDI issues a comprehensive listing of the agents or brokers denied the ability to enter the insurance marketplace or whose licenses have been revoked for character or competency. The *Consumer Alert* is a public record of disciplinary action and is available via the CDI Web site[49] or by calling CDI's Consumer Hotline. *Consumer Alert* is now the third most popular item on the CDI Web site.

Under legislation[50] sponsored by the CDI in 1995, all insurance agents are required to put their license numbers on their business cards and correspondence. With this change in the law, consumers can easily check a producer's license number against those listed in the *Consumer Alert* publication for any possible disciplinary actions.

[47] California Department of Insurance, Field Rating and Underwriting Bureau, March 1999.
[48] California Department of Insurance, Market Conduct Bureau, March 1999.
[49] CDI Website Address: *www.insurance.ca.gov*
[50] AB 702 (Chapter 217/July 1995).

## *Strengthened Surplus Lines Regulation*

California law classifies insurance providers as either *admitted* or *non-admitted*. An admitted insurer is licensed to issue policies to consumers who reside in California. While not formally authorized to transact business in California, as an admitted insurer would be, a non-admitted insurer may be permitted to sell insurance in a restricted manner.

For example, consumers who are unable to purchase the coverage they need from admitted insurers, may be able to obtain the coverage they need from a non-admitted insurer through "surplus lines" insurance. Surplus lines insurance is an important and beneficial supplement to the admitted insurance market because some California consumers may have insurance needs that may not always be met through the admitted (i.e., licensed) insurance market, such as sky-diving insurance or insurance to protect a valuable baseball card collection. For this reason, many consumers need access to specialized coverage that admitted insurers might not offer. To help ensure that consumers have access to financially sound and dependable non-admitted insurers, CDI has implemented safeguards in surplus lines insurance.

### Formation of the LESLI White List

SB 959 (Chapter 980/Sept. 1994) created the **List of Eligible Surplus Line Insurers** (LESLI).[51] The bill set forth minimum qualifications that had to be met by a non-admitted insurer in order for that insurer to be authorized to provide coverage through the surplus lines. The legislation also required CDI to establish a public register of all surplus line insurers that have met the minimum eligibility requirements.

To be eligible, a non-admitted insurer must continually maintain a minimum of $15 million in capital and reserves consisting of assets acceptable under the California Insurance Code.

CDI issued the first LESLI listing on July 7, 1995. The effect is that the surplus lines market has become more restrictive as to the number of non-admitted companies allowed to do business in California. However, because surplus line insurers have to meet minimum qualifications to be eligible for the LESLI list, consumers are better protected.

CDI's involvement in the area of regulating non-admitted insurers also extends nationally. The Commissioner serves as a member of the National Association of Insurance Commissioners (NAIC) Surplus Lines Task Force, which closely monitors the surplus lines market and its operation. The task force also develops model regulations to both protect consumers and promote that market's viability.

Currently, there are over 400 surplus line *brokers* licensed by CDI to negotiate and place insurance with non-admitted insurers.[52] To protect consumers, surplus line brokers are generally prohibited from making placements with any non-admitted insurers that have not been placed on the LESLI list.

## *Reinforced Consumer Services Division*

In 1995 and 1996, CDI faced budget restrictions and was forced to layoff 89 positions, including 47 in the *Consumer Services Division*.[53] The layoff alleviated a pressing budget constraint, but such short-term solutions exacted a long-term price. This was especially true with regard to consumer protection endeavors that could undermine efforts to shield consumers from abusive tactics by insurance providers.

Following the budget crisis, CDI promptly sought to restore the positions in the consumer protection unit and has worked for the passage of SB 18 (Chapter 239/Aug. 1997), which provided funding for the Department to restore positions in the *Consumer Services Division*. In 1998, CDI vigorously sought to increase funding for 27 additional consumer service positions that are fundamental in fighting unfair claim practices by insurers. Efforts to increase CDI's capacity in the *Consumer Services Division* include:

- All 27 positions in the Consumer Services Division and *Market Conduct Bureau* authorized by SB 18 have been filled.
- Increasing *Consumer Services Division* staff by 15 new examiner positions in the 1999/2000 Governor's budget (includes 10 positions in *Market Conduct Bureau* and 5 positions in *Field Rating and Underwriting Bureau*).
- Increase broader review of all types of insurer claims files with additional positions in the *Claims Services Bureau*.[54]

### Use of Information Technology to Protect Consumers

To better serve consumers who called with complaints, the *Consumer Services Division* needs to provide accurate and timely responses to consumers. At the beginning of 1995,

[51] The Surplus Lines Association of California, *Developments in the Regulation of the Surplus Line Industry*, http://www.sla-cal.org/general_SLAlaws-reg/dev-sl.htm.

[52] The Surplus Line Association of California, undated pamphlet.
[53] California Department of Insurance Press Release #028, April 24, 1997.
[54] California Department of Insurance, Responses to Information Requests for the California Senate Insurance Committee Hearing, February 25, 1999.

CDI began aggressively pursuing opportunities in order to be equipped with the latest in consumer protection tools, such as:

- ***Complaints Database System* (CDS):** A nationwide database administered by the National Association of Insurance Commissioners (NAIC) used for referencing and analyzing consumer complaints filed with state insurance departments. Complaints reported to the insurance departments are submitted to the NAIC **CDS** database enabling its member insurance regulators to review this information during market conduct examinations and compare complaint experience with premium volume and other insurance companies.[55]

- ***Producer Database* (PDB)**: A NAIC administered project[56] to provide information relating to insurance agents and brokers (producers). The **PDB** links participating state regulatory licensing systems into one repository of producer information. The PDB will also send an electronic notification to state regulators if administrative action is taken against a licensed producer in their state or if a producer no longer holds an active resident license. The key benefits of the **PDB** are:

  - ♦ Immediate access to disciplinary history nationwide.
  - ♦ Immediate electronic notification of administrative action nationwide.
  - ♦ Ability to verify licensures in good standing in all participating insurance regulatory departments.

- ***Case Management Program*** and an ***Automated Case Management System*** that:

  - ♦ Establishes objectives for all facets of case management, from initial receipt of alleged law violations to the disposition of completed casework.
  - ♦ Enhances management oversight of investigative case activities.
  - ♦ Enhances investigators' planning and reporting of investigative activities.
  - ♦ Improves time management and reporting.

## Y2K Assessments

To protect consumers against possible fallout from the "Y2K bug," CDI initiated a comprehensive program to ensure that insurance providers remain capable of meeting their obligations to policyholders when the Year 2000 arrives. Insurance carriers, producers, and others regulated by CDI have been surveyed and many examined by an independent third party to confirm that prudent steps are being taken to protect policyholders.

Exhaustive steps have also been taken to ensure that CDI, as a business entity within the state government framework, will be prepared internally for the Year 2000.

Furthermore, as a member of NAIC's *Year 2000 Industry Preparedness Task Force* and chair of the NAIC's *Year 2000 Working Group*, CDI participates in nationally coordinated efforts with other states in assessing the industry's state of readiness for the Year 2000. The *Task Force* and *Working Group* provide effective forums to share Y2K-related information among states, such as:

- Current information on specific insurance carrier's state of readiness for Y2K, including contingency plans, compliance costs and external risks.
- Monitoring Year 2000 assessment activities of industry preparedness.
- Providing training and other assistance in developing Year 2000 compliance techniques.

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[55] National Association of Insurance Commissioners, *State Regulation 2000*, Internet site found at http://www.naic.org/consumer/sr2000/sr2000.htm.
[56] National Association of Insurance Commissioners, *State Regulation 2000*, Internet site found at http://www.naic.org/consumer/sr2000/sr2000.htm.

# CRACK DOWN ON INSURANCE FRAUD

Insurance fraud ultimately increases the cost of insurance for everyone and it is usually the responsible, law-abiding consumers that end up paying more in higher insurance premiums. The CDI pursues a broad spectrum of suspected fraud cases ranging from the individual fraudster to well organized fraud rings. Fraud is a crime that is often hard to detect and can be even more difficult to prevent, but there are many things individuals can do to protect themselves from becoming victims of insurance fraud. During 1995 to 1998, CDI greatly enhanced the Fraud Branch's effectiveness by making dramatic improvements to its internal business functions and by introducing several innovative anti-fraud programs.

## *Enhanced Anti-Fraud Capabilities*

Through internal improvements, the Fraud Branch is now in a better strategic position to investigate and pursue fraudulent activities. Examples of internal improvements include:

- An enhanced ability for the Fraud Branch to investigate fraud by streamlining the review, processing and assignment of reported suspected insurance fraud. This enhancement has enabled more efficiency in the processing and investigation of fraudulent claims, allowing the Fraud Division to pursue more cases per year.
- A new case management system was instituted providing the ability to effectively track fraud cases. The system functions as a repository for case information and as a centralized database for case monitoring and resource allocation.
- The Fraud Branch has developed closer relationships with inter-governmental task forces, such as those administered by district attorneys in each county. This has resulted in a dramatic rise in fraud arrests.
- The Fraud Branch also implemented the *Fraud Investigator Development Training Program* for new investigators. This structured training has increased productivity and expertise.

## *Extensive Anti-Fraud Outreach Efforts*

CDI has focused its approach to fight insurance fraud by reaching out to anti-fraud allies, including other law enforcement, the insurance industry, medical and legal professionals, and the public. CDI has used this network of allies to distribute anti-fraud training materials and notify the public and other interested parties that it offers an array of anti-fraud information and educational tools, including formal training, public presentations, *Special Investigations Unit* (SIU) instruction, and public information forums.

For example, CDI developed *Insurance Fraud is a Felony*, a brochure designed to familiarize consumers with common insurance schemes and to help protect them from being victims or unwitting participants in insurance fraud. In addition, the brochure describes how to file a complaint of suspected insurance fraud through the Fraud Branch, or CDI's Consumer Hotline.

CDI also believes that insurance providers must play a major role in consumer protection through effective fraud prevention initiatives. The Fraud Branch encourages insurance companies to take proactive approaches toward detecting fraudulent actions. To assist insurance companies in this endeavor, the Fraud Branch conducted a seminar with insurance company CEO's to educate them on the importance of aggressive SIU programs to detect, investigate, and prosecute insurance fraud activities.

## *Initiated "Operation Storm Watch"*

To better protect consumers from victimization by fraud following natural catastrophes, the CDI Fraud Branch initiated *Operation Storm Watch* task force, an alliance between industry and government agencies.

Originally conceived as proactive preparation for winter 1997 El Niño storms, *Operation Storm Watch* is based upon the principle that the citizens of California should be alerted to and protected from individuals who take advantage of victims of natural disasters.

The CDI Fraud Branch established a four-step action plan to help the *Operation Storm Watch* task force achieve its mission:

1. ***Create deterrence to fraudulent claims activity*** by alerting the public that the impending stormy season could have the potential to make residents and businesses victims of fraud scam artists following any property and casualty claims.
2. ***Garner the support of affected professions*** to assist in the reporting of illicit activities by persons suspected of engaging in fraudulent or unlicensed practices.
3. ***Develop a working plan with governmental entities*** to ensure that reports of fraudulent activity are channeled to the CDI Fraud Branch and/or any other appropriate agency for investigation.
4. ***Create an expedited process for receiving, reviewing and investigating suspected fraudulent claims activity*** by each regional office and/or the task force.

*Operation Storm Watch* was a success. In fact, as a testament to its success, *Operation Storm Watch* was used as a model for federal efforts in combating fraud. Its efforts have led to the arrests of more than 70 individuals in Pacoima, West Hills, Long Beach, San Diego, San Clemente, Monrovia, Placentia, Los Angeles, Bellflower, West Covina, Mission Viejo, Cathedral City, San Bernardino, and Simi Valley. [57] [58]

In the future, Operation Storm Watch will continue to provide valuable assistance in protecting Californians from unscrupulous individuals taking advantage of a devastating natural disaster.

## Fraud's "Most Wanted"

As a tool to fight fraud, CDI instituted consumer information and outreach programs, including Fraud's *Most Wanted,* a publication outlining insurance fraud – *what it is, who is perpetrating it, how to spot it and how to report it*.

Increasing public awareness about fraud helps create more knowledgeable consumers and enhances the CDI's ability to capture the criminals committing fraud. The dissemination of anti-fraud material, like the *Most Wanted* and the Fraud Branch's informative magazine, called *Undercover*, has generated numerous questions and responses from the insurance industry and other law enforcement agencies. The sharing of information can lead to insurance fraud referrals and the capture of the fugitives. CDI now even produces *Busted!, a* publication listing fraud arrests each month.

Perhaps the most potentially powerful informational outreach innovation is the use of the CDI Internet Web site as a fraud-fighting tool, providing CDI fraud investigators with an inexpensive way of reaching millions of individuals throughout the world, demonstrating that fraudulent insurance claims are being aggressively investigated and prosecuted in California. According to CDI's Web site traffic statistics, the *Most Wanted* page has become one of the most popular pages. A click on the *Most Wanted* page provides the public with a photograph of the individual suspected of fraud, a brief biography, and other pertinent information.

Thanks to these efforts consumers today have more information than ever before about fraud indicators and other information, such as how to notify CDI of suspected fraudulent claims.

## Workers' Compensation Fraud

In July 1996, CDI's Fraud Branch and the San Diego County District Attorney's Office formed a *Premium Fraud Strike Force*. The goal of this strike force was to identify, investigate, and prosecute individuals and entities that under-insure workers' compensation benefits and commit workers' compensation insurance fraud. To give the *Strike Force* broad experience and expertise, members of the strike force also include investigators and auditors from the State Franchise Tax Board, the Employment Development Department, the Department of Industrial Relations, and the State Contractors Board. The strike force has helped yield timely and efficient criminal investigations of workers' compensation fraud.[59]

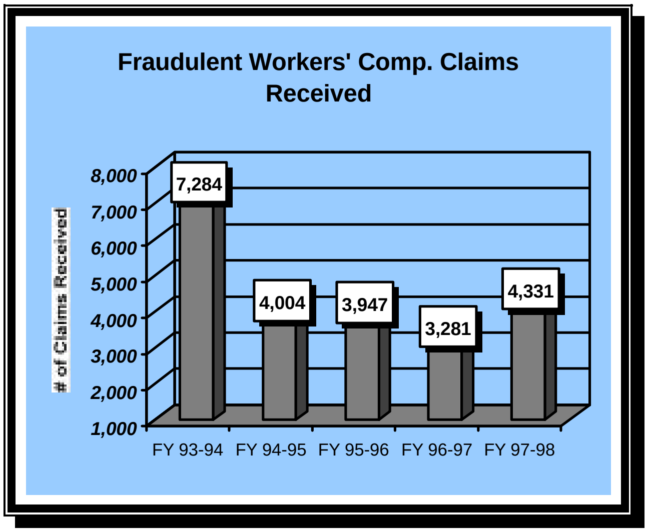
In addition to the efforts of the strike force, the CDI has increased enforcement and prosecution of both claimant and medical providers who file false workers' compensation claims or inflated medical bills. The number of fraudulent workers' compensation claims has diminished substantially since 1993, as demonstrated in *Exhibit 14*. During fiscal year 1993-94, the Fraud Branch received 7,284 suspected fraudulent complaints. In contrast, during fiscal year 1997-98, the Fraud Branch received 4,331 fraudulent complaints.

CDI's tougher enforcement – including more comprehensive investigations by the *Premium Fraud Strike Force* – has produced heightened awareness of workers' compensation fraud activities and has likely contributed to the decreased number of suspected fraudulent claims between 1993-1998.

[57] California Department of Insurance, Fraud Branch, April 14, 1999.
[58] California Department of Insurance, Internet article, *Operation Storm Watch: Watching the Weather and the Crooks.*

[59] California Department of Insurance, Fraud Branch, April 14, 1999.

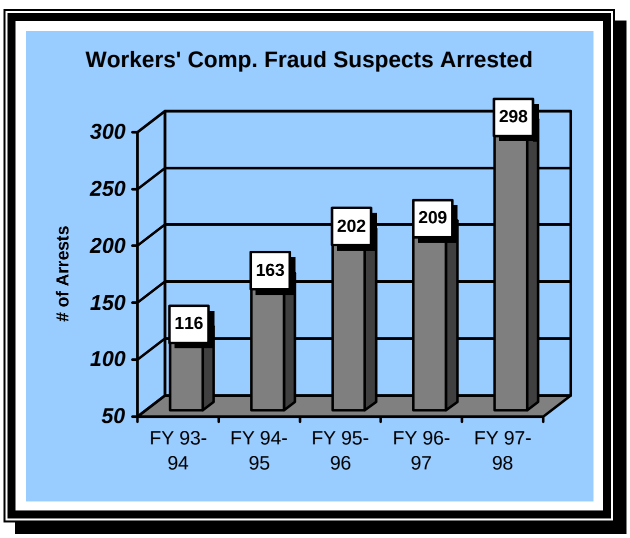
***Exhibit 14: Fraudulent Workers' Compensation Complaints Received***




Source: California Department of Insurance, Fraud Branch, 1999.

Also significant, the number of arrests of workers' compensation fraud suspects has increased steadily over the past four years. In fact, between 1993 and 1998 fraudulent workers' compensation claims have more than doubled – from 116 arrests in 1993-94 to 298 arrests in 1997-98, as *Exhibit 15* illustrates.

***Exhibit 15: Workers' Compensation Program: Suspects Arrested, 93 – 98***




Source: California Department of Insurance, Fraud Branch, 1999.

## *Increased Enforcement and Deterrence Against Auto Fraud*

Statistics gathered by CDI's Fraud Branch show that 14,500 suspected auto-related fraud cases were reported in fiscal year 1998, an increase of approximately 25% from just two years prior and up over 130% since 1990.[60] CDI places a high priority on fighting auto insurance fraud, as CDI's efforts to pass SB 334 (Chapter 189/July 1998)[61] demonstrate. In addition to the work against staged auto collisions, CDI developed a *Local Assistance Program*, working with county district attorneys to aggressively investigate and prosecute criminals who perpetrate other types of automobile insurance fraud.

In recent years these efforts have produced excellent results. During fiscal year 1997-98, there were 751 arrests and 630 convictions of individuals who committed staged auto collisions and attempted other types of auto insurance fraud; ***an 83% conviction rate***! In contrast, between 1988 and 1992 the number of perpetrators convicted of automobile insurance fraud numbered less than 100.

In 1998 CDI's emphasis on punishing auto insurance fraud resulted in the crackdown of the largest international auto insurance fraud scheme in CDI's history, with the arrest of over 70 suspects.

This fraud ring was responsible for illegally shipping over 100 luxury cars to Hong Kong for resale in the People's Republic of China where they would be re-sold at three times their U.S. market value. The suspects first purchased, rented, or leased the cars with an estimated market value of $50,000 each, then insured and shipped them. While the cars were en route to China, the suspects reported to law-enforcement authorities that the cars had been stolen and filed fraudulent claims worth an estimated $4 - 6 million[62] with U.S. insurers.

It took CDI fraud investigators over two years, four-statewide sweeps and extensive coordination with several other government agencies to crack this auto fraud ring.

### Staged Auto Collisions

CDI is most vehement about attacking auto fraud because this particular type of fraud can produce such potentially deadly consequences at the hands of criminals who intentionally maneuver their vehicle into a collision to make it appear that the other driver, often an insured elderly person, is at fault.

[60] California Department of Insurance, Fraud Branch, "Undercover" Vol. 1, No. 3, September 25, 1997.
[61] d affordable for all drivers.
SB 334 (Chapter 189/July 1998) – Fraudulent Auto Accidents, Page 12
[62] California Department of Insurance Press Release #003, January 6, 1998.

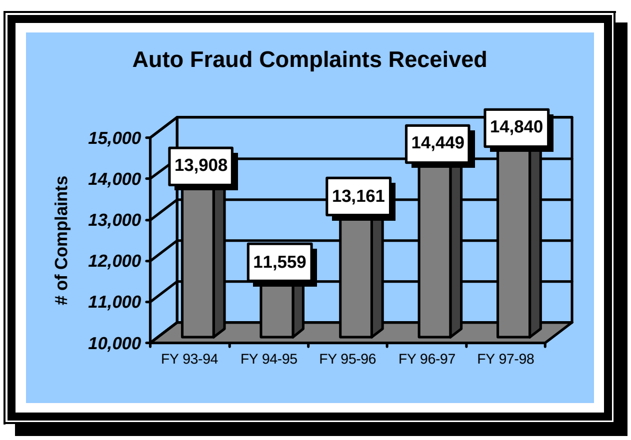
As mentioned previously, SB 334 (Chapter 189/July 1998) increased the penalties that district attorneys can seek against those suspected of staging auto accidents. The bill created new felony sentencing enhancements not only for repeat insurance fraud offenders, but additional penalties if innocent parties suffer serious bodily injury resulting from a staged auto collision.[63]

Sophisticated organized crime rings typically involving attorneys and medical personnel who collaborate by processing fraudulent claims usually carry out staged auto accidents. These "choreographed" accidents often produce numerous injuries and can even be fatal for innocent victims. In a particularly tragic case, a staged auto collision on the I-710 freeway in Los Angeles caught a vehicle containing an innocent Long Beach family, causing the victims' vehicle to burst into flames, killing all of the occupants, including their two-year-old daughter.

But CDI's efforts to prosecute those who run staged auto collision rings have been significant. In fact, CDI has made over 86 arrests in what is referred to as the "Panther" case, allegedly involving the Panther Automotive Center in Garden Grove, California, as the center of a massive staged auto collision ring intended to defraud multiple insurance companies.[64]

Statistics indicate that, while the CDI is working hard to reduce auto fraud in California, the Fraud Branch has a significant challenge ahead. In the past five years, suspected fraudulent complaints have risen slightly. In fiscal year 1993-94, CDI received 13,908 suspected fraudulent claims. By fiscal year 1997-98, CDI received 14,840 fraudulent claims. These statistics are shown in *Exhibit 16*.

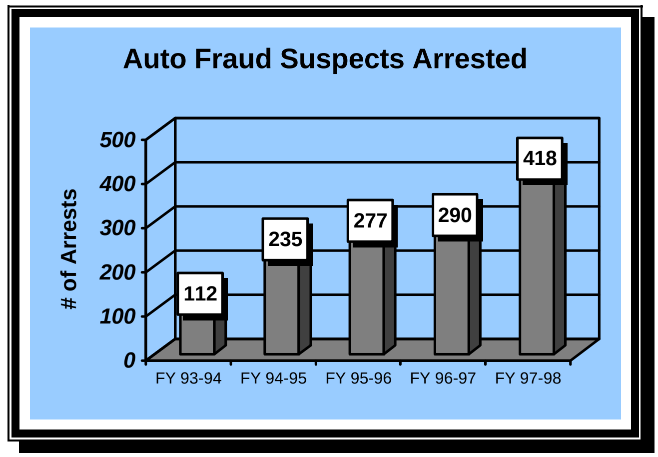
***Exhibit 16: Fraud Branch: Fraudulent Automobile Complaints Received***




Source: California Department of Insurance, Fraud Branch, 1999.

While auto fraud complaints have increased only moderately, the number of arrests in the automobile fraud program has almost **tripled** since 1993-94. In 1993-94, CDI arrested 112 suspects. Four years later, CDI made 418 arrests, as shown in *Exhibit 17*. In order to send the clear message that fraudulent claims and practices are taken very seriously, CDI has heightened enforcement and prosecution against fraudulent auto insurance claims.

***Exhibit 17: Fraud Branch: Automobile Fraud Suspects Arrested***




Source: California Department of Insurance, Fraud Branch, 1999.

## *Increased Enforcement and Prosecution of Other Types of Fraud*

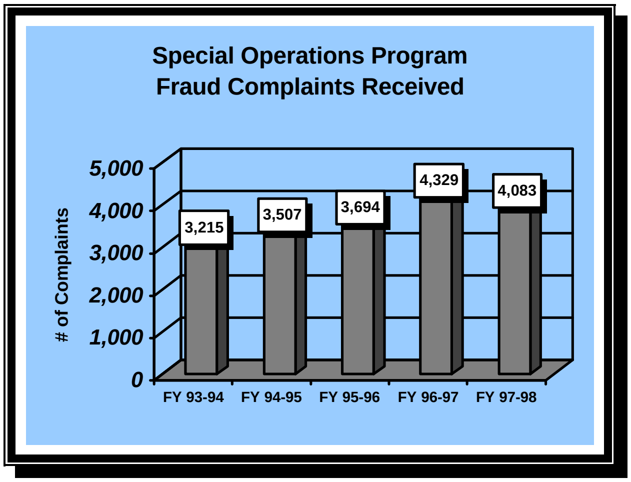
CDI's initiatives to protect consumers against fraud also include increased investigation and prosecution against other types of fraudulent property claims. CDI's *Special Operations Program*[65] is responsible for investigating fraudulent claims that include:

- Property (theft and vandalism)
- Life and health
- Burglary (residential and business)
- Slip and fall
- Medical
- Pharmacy
- Dental
- Embezzlement
- Disability
- Arson

In the past five years, the *Special Operations Program's* workload has risen. In 1993-94, it received 3,215 suspected fraudulent claims. By 1997-98, it received 4,083 fraudulent claims.

[63] California Department of Insurance, Fraud Branch, April 14, 1999.
[64] California Department of Insurance, Fraud Branch, April 14, 1999.
[65] California Department of Insurance, Fraud Branch, April 14, 1999.

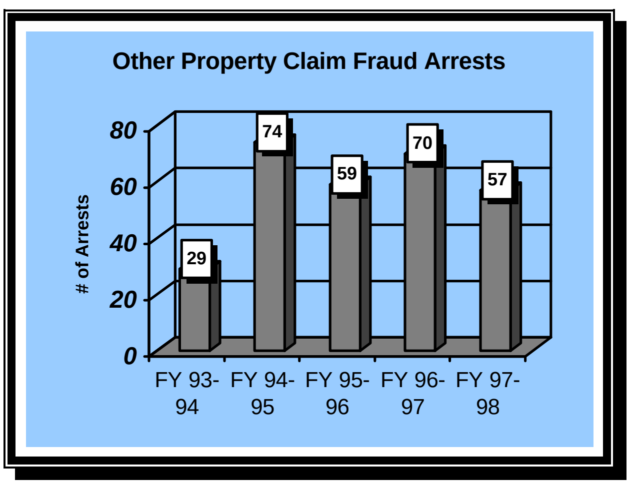
*Exhibit 18: Suspected Fraudulent Complaints to the Special Operations Program.*




Source: California Department of Insurance, Fraud Branch, 1999.

While the number of claims has increased by 25% during 1995 to 1998, the number of arrests in the *Special Operations Program* has increased since 1993-94. In fiscal year 1993-94, the *Special Operations Program* arrested 29 suspects. In fiscal year 1997-98, the *Program* made 57 arrests. It is hoped that greater numbers of arrests and prosecution will produce a deterrent effect and reduce the frequency of fraudulent property claims.

*Exhibit 19: Other Property Claim Fraud Suspects Arrested*




Source: California Department of Insurance, Fraud Branch, 1999.

## Audits of Insurers' Anti-Fraud Units

CDI has greatly increased the auditing of insurance companies to ensure that they maintain effective anti-fraud insurance units.

In 1998 CDI issued *Orders to Show Cause* to two insurance carriers to explain why their *Certificate of Authority* should not be suspended for failing to maintain anti-fraud units. Both carriers subsequently stipulated to the Department's order to maintain sufficient anti-fraud units, paid fines totaling $80,000, and are currently being monitored and re-inspected to ensure their compliance.[66]

## Participated in National Anti-Fraud Efforts

CDI is a member of the National Association of Insurance Commissioner's *Anti-Fraud Task Force*. The purpose of this task force is to serve the public by assisting state insurance regulators in fundamental anti-fraud activities:

- Promotion of the public interest through the detection, monitoring, and appropriate referral for investigation of insurance crime by both consumers and insurance providers.
- Assistance to the insurance regulatory community through the maintenance and improvement of electronic databases tracking fraudulent insurance activities.
- Research and analysis of insurance fraud trends and case-specific analysis to insurance regulators and state and federal law enforcement agencies.
- Provide a liaison function between insurance regulators, law enforcement and other specific anti-fraud organizations.[67]

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[66] California Department of Insurance, Fraud Branch, April 14, 1999.
[67] National Association of Insurance Commissioners, 1999 Committee Charges, Adopted February 8, 1999.

# CDI'S EFFICIENCY AND EFFECTIVENESS

## *Instituted the Consumer Ombudsman as Problem-solver for the Public*

The Ombudsman's Office was originally established to help the average citizen navigate CDI. Today, the Ombudsman continues to serve the public in providing "2nd review" problem-solving for the public and public officials, such as legislators to whom the public often turns for assistance. Because of the key role the Ombudsman's Office plays as intermediary between the public and CDI, the Ombudsman is often in a position to help identify and develop innovative ways of serving the public better.

The Ombudsman's Office works to improve communications throughout CDI and coordinate the quality and accuracy of information being given to consumers. In many cases, multiple bureaus or divisions within CDI were working on the same case or issue with no knowledge of the other units' efforts. To correct this deficiency, the Ombudsman implemented measures, including an *Intranet*, to facilitate information exchange throughout CDI's various units. This effort allowed CDI to identify trends in certain issues and work across divisional lines to effect policy or procedural changes.

Since its inception, the Ombudsman's Office has fielded thousands of inquiries, currently handling well over 100 cases and 600 inquiries each month.[68] The office is uniquely positioned to resolve even the most complex cases.

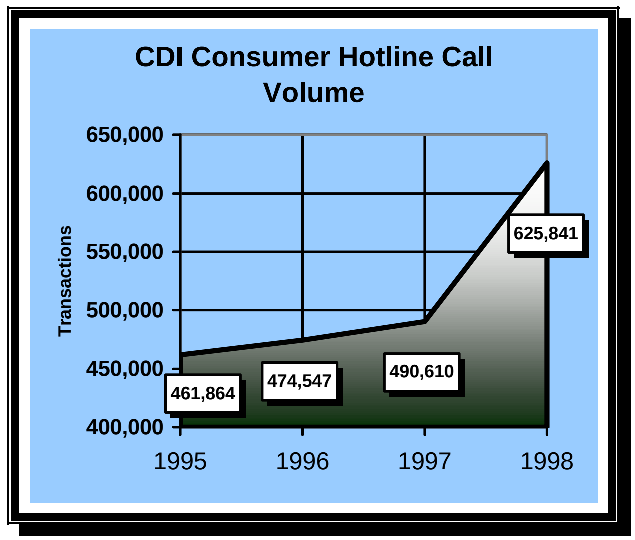
In addition to helping consumers settle their cases, the Ombudsman's Office attempts to create an environment within CDI that is more customer-friendly. For example, the Ombudsman worked to consolidate public counters in CDI's main offices to reduce the "run-around" consumers often experienced when seeking information. The Ombudsman also developed procedures for better serving customers who arrived at public counters without an appointment.

## *Modernized CDI Consumer's "Hotline"*

When consumers have a question about any insurance-related question, they can contact the CDI's *Consumer Communications Bureau*. This bureau, also known as the CDI ***Consumer Hotline***,[69] is responsible for handling incoming phone calls as well as written communications.

Since 1995 the volume of consumer transactions handled by the ***Consumer Hotline*** has been steadily increasing. For example, **in 1995 approximately 462,000 transactions were handled and in 1998 there were nearly 626,000 transactions**. Several factors could attribute to this increase, including the passage of a law that requires CDI's phone number be printed on all insurance policies and growing consumer interest. *Exhibit 20* illustrates the increase in calls to the Consumer Hotline.

***Exhibit 20: Increasing Call Volume for the CDI Consumer Hotline***




Source: CDI , Consumer Communications Bureau, memorandum dated April 13, 1999.
Note: Workloads were not fully known during 1991-1994 due to incomplete tracking.

At the same time, as call volumes are steadily growing, the substance of the calls is becoming more complex. Customers who called during 1995 and 1998 sought information about issues such as Proposition 103, and assistance regarding natural disasters like earthquakes and fires. Efforts to provide the *Consumer Communications Bureau* with additional resources, such as implementing new systems and procedures, and increased staffing of the ***Consumer Hotline*** to deliver information and service to consumers

[68] California Department of Insurance, Office of the Ombudsman, 1999.

[69] CDI's Consumer Hotline (800) 927-HELP or (213) 897-8921

more quickly, has raised the standards of customer service to its highest levels in the Department's history.[70]

Over the course of 1995 to 1998, the *Consumer Communications Bureau* implemented new procedures and systems, such as:[71]

- Increased ***Consumer Hotline*** staff to expand problem-solving resources for the public.
- Expanded the number of service choices available to consumers when they call the ***Consumer Hotline***.
- Updated and increased the number of brochures and pamphlets available to consumers.
- Partnered with the State Controller's Office to assist consumers in obtaining Proposition 103 rebate funds that had been escheated to the state.
- Expanded the *Consumer Outreach Program* in 1997 to include senior citizen insurance abuse forums and education forums designed to address fraud scams in the aftermath of El Niño.
- Implemented the *Integrated Database System* and *Intelligence Gathering System*.

Because of new resources, systems, and processes, the ***Consumer Hotline*** is now better equipped to respond to the needs of California's consumers. Indeed, satisfaction surveys for 1998 indicate that 86% of all consumers who contact the CDI would recommend the Department to others, and 79% believe their problem was resolved satisfactorily.[72]

## *Improved Administrative Responsiveness*

California has become a more competitive insurance market because, in part, CDI is more responsive than in the past, acting as a facilitator of competition in the market, rather than an impediment. This is what CDI refers to as "good government." To accomplish this, CDI has endeavored to be more efficient in the process of admitting insurers, reviewing forms and approving rates through the appropriate use of automated technology, instituting streamlined processes, and conducting operational efficiency reviews. In fact, this effort has resulted in tangible benefits to California consumers in terms of timesavings and reduced costs. Through enhanced competition and increased availability of insurance products in the California marketplace, consumers ultimately benefit from higher quality insurance products at lower rates.

### Cutting the "Red Tape"

Through initiatives to reduce much of the "red tape" commonly associated with government bureaucracies, CDI has made it easier for insurers to enter and compete in the California marketplace. During 1995 and 1996, CDI authorized 111 new companies to operate in California, compared with 71 during 1993 and 1994. During 1993 and 1994, 21 companies stopped doing business in California, compared to just 12 during 1995 and 1996. In total, 120 more companies have been brought into California since 1995, which left California for nine years following the passage of Proposition 103 in 1988.

### Thorough Policy Form and Rate Approval

State regulation of insurers normally requires policy form and rate approval.[73] These regulations are critically important because insurers normally dictate the terms and conditions of their insurance policies. The consumer, on the other hand, generally has less expertise in insurance matters and has less information about whether a policy is written fairly. CDI considers the fair and equitable treatment of the insured in the insurance transaction to be of utmost importance. For this reason, insurers must obtain approval for the products they seek to sell and, specifically, the policy forms that they use so CDI can ensure that policy provisions are reasonable and fair and do not contain major gaps in coverage that might be misunderstood by consumers.

[70] Budget problems during 1996 resulted in the cutbacks of 89 staff positions, which affected the Consumer Services Division. In 1997, CDI sought and received funding from the Legislature to reverse the layoffs and hire 27 individuals within the Consumer Services Division to work directly with consumers.

[71] California Department of Insurance, Consumer Communications Bureau Management Staff, memorandum dated April 13, 1999.

[72] California Department of Insurance, Consumer Communications Bureau Management Staff, memorandum dated April 13, 1999.

[73] CDI's review of insurance rates is governed, in part, by the requirements in the California Insurance Code (CIC) Section 1861.05 and California Code of Regulations (CCR) Title 10, Subchapter 4.8, Article 1, Sections 2641.1 through 2644.23. California Insurance Code Section 1861.05 (a) states, in part: "No rate shall be approved or remain in effect which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter." CCR Title 10, Subchapter 4.8, Article 1, Sections 2641.1 through 2644.23 provide the definitions for "excessive" and "inadequate" as well as the various ratemaking formulae to be used by the CDI when reviewing an insurer's filed rate indications and selections. These are commonly referred to as the *Prior Approval Regulations*.

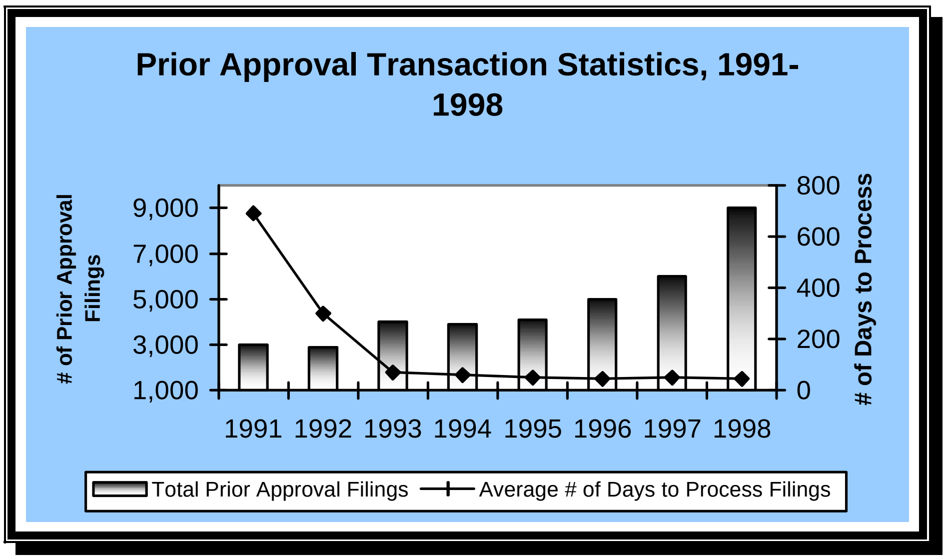
## Fairness in Rate Regulation

Another important role for CDI is rate regulation. When choosing a policy, the consumer is not usually in a position to determine the fairness of the premium for the policies they purchase. Rate regulation ensures that insurers' rates and premiums are adequate (sufficient to maintain solvency), not excessive, and not unfairly discriminatory.[74] However, CDI recognizes that an inefficient rate filing approval process can stifle creativity in the marketplace, dampening insurers' interest in responding to the public's need for insurance products.

Since 1995, beneficial changes in management direction and the introduction of automation have resulted in a rate and form review process that is noticeably streamlined. different management emphasis. Other contributing factors include increased experience of the insurers in submitting more complete rate applications, increased understanding of the filing process and clearer and more complete regulations in place directing the filing and review process.

Besides the improvements to the rate and form filing process, **rate filings received after 1994 have tended to be rate *decreases***. Therefore, a higher percentage of the rate filings were non-controversial, requiring less negotiation with insurers delaying the approval process. Prior to 1995, CDI was immersed in the Proposition 103 rollback and rebate process and approval of rate filings was often linked to settlement of rollback issues.

***Exhibit 21: Prior Approval Transaction Statistics, 1991-1998***




Source: California Department of Insurance, Rate Regulation Branch, 1999.

## Faster Regulatory Processing

CDI has diligently sought to perform its duties more responsively and timely and has vastly improved its deference for its consumers, resulting in faster processing and turnaround times for policy approvals, rate filings, and applications review. For instance, in January 1995, there were 2,044 files awaiting review by CDI's Legal Branch, *Policy Approval Bureau*, some dating back as much as four years. By January 1, 1997, the backlog had been reduced to only 155 files, the oldest being only six months.[75] As *Exhibits 21 through 23* document, the number of days required to review forms and applications has dramatically declined even as the volume of transactions increased significantly.

*Exhibit 21* summarizes statistics for "Prior Approvals,"[76] which refers to all filings handled by CDI's *Rate Regulation Division*. As noted, the average number of days to process prior approval filings decreased as the total number of filings increased steadily between 1994-1998. The *Rate Regulation Division* attributes this increased efficiency to more extensive and sophisticated use of information technology, along with a more experienced workforce and a

Processing times for rate filing applications have been reduced from a high of two years to the current 30 to 90 days. In 1994, there was a frequent problem of approving rate filings within the 60-day "deemer" window. That problem no longer exists. *Exhibits 22 and 23* document the efficiency trends of rate filings: rate increases, rate decreases and new program filings.

As *Exhibit 22* shows, the numbers of rate decrease filings from insurers doubled in 1996 and doubled again by 1998. Despite this significant workload increase between 1994 and 1998, CDI's *Rate Regulation Branch* was able to review each filing in less than 100 days.

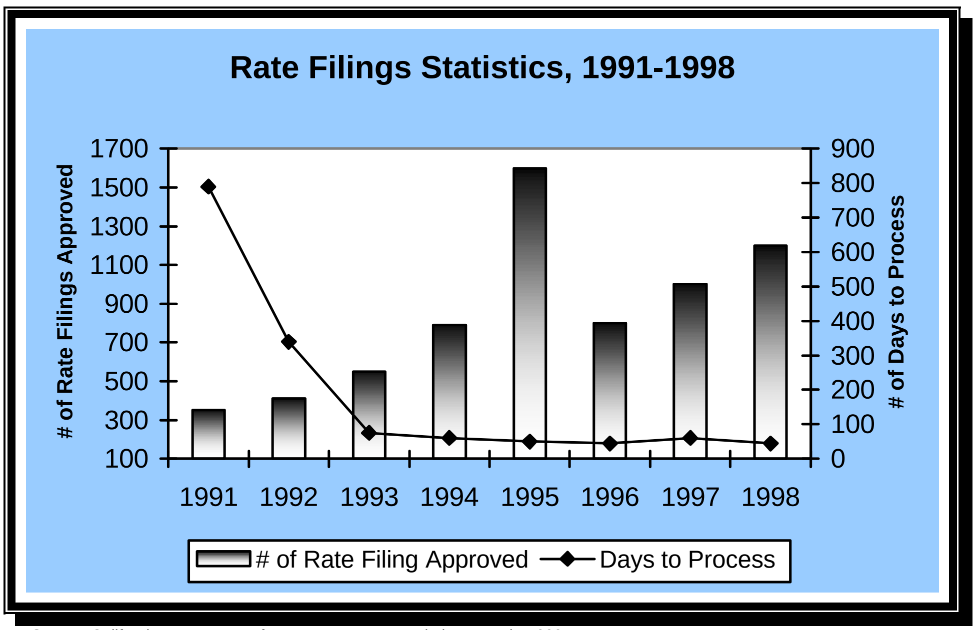
*Exhibit 23* shows that CDI was able to maintain its efficiency in reviewing new program filings even while the workload volume grew significantly from 1995 to 1998.

[74] California Insurance Code Section 1861.05(a)
[75] California Department of Insurance, 1998
[76] California Insurance Code, Section 1861.05(b)

## Friendlier Business Environment for Insurers Seeking to do Business in California

At times, new programs are filed in conjunction with a *Certificate of Authority* application, but normally a new program filing represents a licensed insurer's proposal to enter a new market niche (i.e. a line or class of where the insurer has not previously been active). CDI evaluates new programs to verify that the proposed rates are reasonable for the coverage provided and are not excessive, inadequate or unfairly discriminatory.

***Exhibit 22: Rate Filing Statistics Demonstrating Improved Efficiency, 1991-98***




Source: California Department of Insurance, Rate Regulation Branch, 1999.

Even as CDI's review and approval process was streamlined, CDI worked to make sure that insurance providers clearly understood the steps involved in the regulatory process. In addition, CDI has worked to revamp the applications for companies that wish to transact insurance in California and improved the Department's licensing (Certificate of Authority) process.

**The revised application dramatically reduces the time required for review, from a typical two-year review period to a maximum review period of <u>only 90 days</u> for complete applications**. Streamlining the *Certificate of Authority* process and other improvements translate into increased competition in the California insurance marketplace. Indeed, during 1995 to 1998, CDI licensed over 133 <u>new</u> insurers and another 127 insurance-related companies.[77]

CDI's regulatory divisions and the Ombudsman's Office deserve the credit for helping to streamline the process through which insurers gain entry into the California market by providing better assistance to insurers as they entered this process. Examples of efforts to assist insurers include:

- **Producer licensing reform –** improved CDI's licensing function, introduction of the Interactive Voice Response (IVR) telephone system, *License Inquiry System* availability on CDI's Web site, hired an Assistant Ombudsman to assist the producer community, established an *Agent and Brokers Advisory Committee* (ABAC) and created a producer newsletter, *Communiqué*.
- **ALERT –** CDI is providing leadership in the *Accelerated Licensure Evaluation and Review Techniques* (ALERT) Project that seeks to streamline and standardize the company admissions process for all states through NAIC.

## Progressive and Forward Thinking

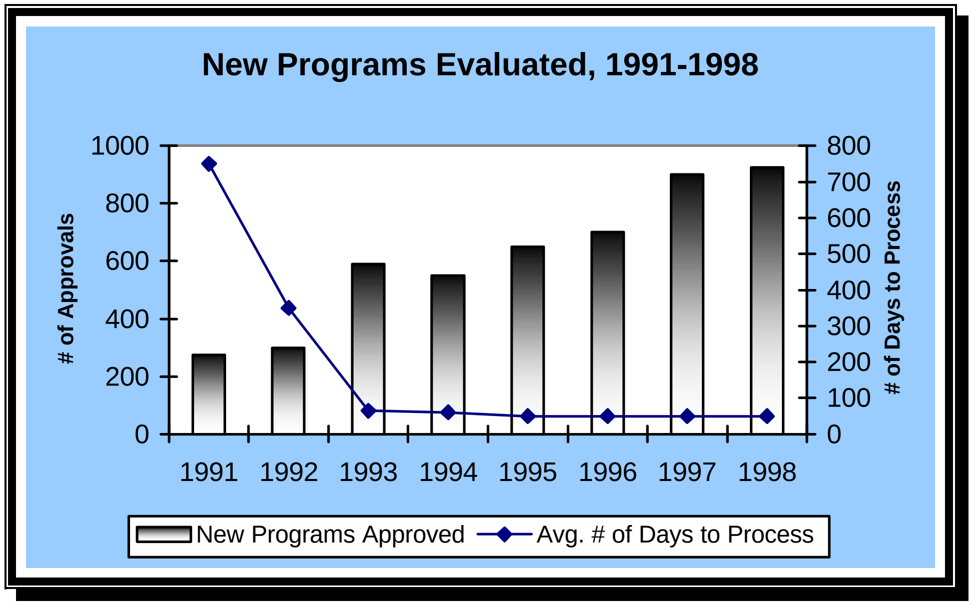
CDI does not believe that its role as regulator of insurers necessarily has to be adversarial. The Department has worked to maintain good relationships with the industry and has proactively recruited several insurers into the California market including several large insurance companies. In some cases, the strategy actually had CDI "cold-calling" the CEO's of carriers not admitted in California. Several of them reported that they had never heard of a Department being so progressive.[78]

[77] California Department of Insurance, Rate Regulation Branch, May 18, 1999.
[78] California Department of Insurance, Office of the Ombudsman, March 11, 1999.

## Instituted New Automated Systems

CDI has pushed hard to introduce advanced information technologies (IT) that would enhance its ability to provide oversight of insurers and quality services to California's consumers. Through strategic IT planning, creating an IT infrastructure, and implementing best practices in managing the investment in IT, CDI has been able to empower employees to be more effective. *Exhibit 24* summarizes some of the major accomplishments.

***Exhibit 23: New Programs Evaluated, 1991-1998***




Source: California Department of Insurance, Rate Regulation Branch, 1999.

The new technology and systems for the management and oversight of critical regulatory functions, including market conduct oversight, and insurer and agent case reviews are now being performed more efficiently and effectively than ever before. In addition to CDI's IT initiatives, the Department is working with NAIC to develop automated national systems to streamline the oversight and administration of insurance companies. Two projects being implemented in cooperation with NAIC are: [79]

- **System for Electronic Rate and Form Filings (SERFF)**[80]
  SERFF enables insurers to submit rate and form filings electronically to state reviewers, reducing the time and cost involved in making regulatory filings. State reviewers use SERFF to facilitate the management, analysis, disposition and storage of the filings. Both insurers and regulators benefit from the electronic communication that SERFF provides. SERFF is unique in that it is a joint, cooperative initiative between regulators and industry.
- **Uniform Certificate of Authority Application**
  Designed to allow insurers to file copies of the same application for admission in numerous states. While each state still performs its own independent review of each application, the need to file many different applications, in different formats, has been eliminated for each state that accepts the Uniform Certificate.

## Comprehensive Reviews of CDI Operations

By 1995, CDI's management controls and operations had been seriously degraded. In June 1995, as CDI was in the process of closing its books for fiscal year 1994-95, the California Department of Finance was requested by the Commissioner to perform a priority audit of CDI's accounting systems and fiscal controls.

The Department of Finance's audit led to a major effort to stabilize CDI's fiscal condition and controls. As it turned out, many of the Department of Finance's findings had already been documented by at least two previous audits performed by the State Controller's Office in 1991 and 1993. In 1995 CDI proceeded to correct the pre-existing management control issues.

During this improvement effort, the State Auditor conducted an audit and identified a number of serious fiscal management problems within CDI. The vast majority of these audit findings were carryover issues from previous audits, which had essentially been ignored by previous administrations. All audit findings have since been addressed as a result of CDI's implementation of comprehensive fiscal controls and internal system checks. The steps implemented overcame the fiscal management problems encountered in 1995. *Exhibit 24* provides examples of the types of problems that existed in CDI, and what has been

[79] National Association of Insurance Commissioners, *State Regulation 2000 Initiative* (http://www.naic.org/consumer/sr2000/sr2000.htm)
[80] National Association of Insurance Commissioners, *SERFF Virtual Brochure* (http://www.serff.org/serff/brochure/virtual_brochure.htm)

done to correct them. *(For more examples, see Exhibits 27, 28, and 29 in the Appendix)*

***Exhibit 24: Major Administrative Accomplishments, 1995 - 1998***

| THEN (1995) | ➔ | NOW (1998) |
|---|---|---|
| **Information Technology** | | |
| ▪ No Departmental review or prioritization of IT resources | ➔ | ▪ IT Policy Committee provides Executive level prioritization. |
| ▪ Manual work processes | | ▪ Automated efficiency |
| ▪ No internet/intranet | | ▪ CDI internet/intranet. Higher customer service and satisfaction. |
| **Administration Systems** | | |
| ▪ Inaccurate and misallocated expenditures to programs. | ➔ | ▪ Revamped cost allocation system. |
| ▪ No standard billing system | | ▪ Implementation of ORACLE Financials |
| **Human Resources** | | |
| ▪ CDI provided "free" loans to employees. For example, one employee received $10,000 in salary advances with $100 monthly payback. | ➔ | ▪ Enforced strict adherence to State Administrative Manual (SAM) procedures. |
| ▪ Employees were routinely overcompensated for working out-of-state as much at $200 - $500 per month per employee. | | ▪ Enforced strict adherence to Department of Personnel (DPA) rules regarding out-of-state compensation. |
| ▪ Department did not have policy on discrimination in compliance with EEO regulations | | ▪ Policy and procedures addressing discrimination. |

Source: California Department of Insurance, Administration Branch, 1999

CDI has implemented sound fiscal controls to ensure adequate personnel timekeeping, accounts receivable, financial reporting, and cost allocation. These essential activities will help ensure the accountability and effective long-term financial management of CDI's activities.

CDI has also worked to address the shortcomings identified by state oversight agencies regarding CDI's human resources functions. *Exhibit 29* in the Appendix summarizes how CDI's human resources-related problems were addressed.

CDI has also addressed the severe and chronic structural deficiencies in its fiscal management by initiating plans to strengthen the staffing, systems, and processes involved in fiscal operations. *Exhibits 30 through 32* in the Appendix summarize the corrective measures implemented in the *Business Services Management Bureau*, the *Accounting Office*, and the *Budget Office*.

CDI has also upgraded accounting and budgeting functions, summarized in *Exhibits 30 and 31*. In the accounting area, CDI has ensured the hiring and retention of qualified staff, the development of sound policies and procedures, the redesign of processes to enhance efficiency and accountability, and the implementation of automated tools reflecting the best practices currently available in financial management. These steps are summarized in the Appendix, *Exhibit 30*.

In addition to instituting major improvements within CDI's Administration Branch, CDI had independent assessments conducted on a number of its Divisions to ensure that the agency was protecting and serving consumers in the most efficient and effective manner. *Exhibit 25* summarizes the types of independent reviews of CDI's efficiency and effectiveness.

***Exhibit 25: Independent Review of CDI Operations***

| Focus of Review | Review Completed |
|---|---|
| **Consumer Communication Bureau "Hotline" Implementation Project** | January 1996 |
| **Strategic Assessment of CDI's field Operations** | July 1996 |
| **Strategic Assessment of Legal Branch** | October 1996 |
| **Field Operations Implementation Project** | January 1997 |
| **Review of Fraud Branch** | November 1997 |
| **Review of the Market Conduct Examination Process** | November 1997 |
| **CDI's Strategic Plan** | October 1998 |
| **Administrative Law Bureau: Organizational Review.** | January 1999 |

Source: KPMG Consulting, March 1999

Through the recommendations developed during the course of these reviews, CDI was able to make numerous changes to its organization and operation. Of course, like any organization, CDI continues to improve its operational efficiency and effectiveness. During a performance audit of its operations in early 1997 the Bureau of State Audits' report found several areas in need of improvement.[81] Within one

[81] California Bureau of State Audits, "Department of Insurance: Management of its Financial Affairs and Programs Needing Improvement," 1997.

year, most of the State Auditor's recommendations had been completed, demonstrating management's desire for quick responsiveness and immediate corrections to legitimate problems.[82]

## *National Leadership in Insurance Regulatory Improvements*

CDI provides leadership on many national insurance regulation issues and participates in numerous committees and task forces of the NAIC, including:[83]

- **Special Committee on Regulatory Re-Engineering (EX)** – Provides information about state regulatory re-engineering initiatives and encourages states to replace outdated regulatory processes. Implements an awards program to recognize states for involvement in regulatory re-engineering initiatives. Evaluates the Internet and other means of electronic commerce to increase efficiency. Harmonizes state laws, regulations, and procedural requirements governing the insurance industry. Maintains and improves appropriate consumer protections.
- **Financial Condition Subcommittee (EX4)** – Provides a central forum and acts as coordinator of solvency-related considerations of the NAIC relating to accounting practices and procedures, blanks, valuation of securities, the *Insurance Regulatory Information System* (IRIS), financial analysis and solvency, zone examinations, and examiner training.
- **Blanks Task Force (EX4)** – Considers improvements and revisions to the various blanks and conforms these blanks to changes made in other areas of the NAIC to promote uniformity in reporting of financial information by insurers; explores the feasibility of electronic filing vs. hard copy filing of various parts of the annual statements to reduce unnecessary printing and filing costs incurred by insurance companies. Continues to monitor the quality of financial data filed by insurance companies. Develops proposals for implementing standard formats and filing requirements for all business types, reducing the reporting burden on insurance companies.
- **Examination Oversight Task Force (EX4)** – Monitors the financial examination process and identifies, investigates, and develops solutions to problems related to financial examinations. Monitors usage of automated examination tools, technology changes, and emerging issues.
- **Financial Database Re-Engineering Task Force (EX7)** – The FDR Task Force of NAIC's Information *Services Subcommittee* provides oversight for the Financial Database Re-engineering Project, ensuring that resources of the NAIC are appropriately deployed in such a manner as to re-engineer financial database systems and business processes to:
    1. Meet or exceed business requirements not currently being met.
    2. Improve the flexibility, efficiency, and cost-effectiveness of current systems.
    3. Reduce the cost of regulatory compliance in the area of financial reporting.
    4. Explore alternative methods of filing financial statements through the Internet.
- **NAIC/AAA/ASB/ABCD Joint Committee** – Provides a conduit between the regulatory actuaries of the NAIC, the American Academy of Actuaries, the Actuarial Standards Board, and the Actuarial Board for Counseling and Discipline.

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[82] California Department of Insurance, Audit Program Division, 1999.
[83] National Association of Insurance Commissioners, 1999 Committee List: Committee, Subcommittee, and Task Force Assignments, January 27, 1999.

# CONSUMER PROTECTION

One of the fundamental goals of state insurance regulators is to closely monitor the financial integrity of the insurance industry and protect consumers and others against insurer insolvency. Despite regulators' best efforts, however, financially troubled insurance companies can become bankrupt.

In the past, CDI's ability to protect the interests of consumers against insurer insolvency was severely handicapped. Mismanagement and ineffective operations in CDI's Conservation and Liquidation Office plagued CDI for many years. One of the most notable achievements for CDI has been to restore its ability to undertake sound regulatory actions with respect to troubled companies by addressing and correcting these problems.

CDI's efforts have directly resulted in providing greater returns to policyholders from liquidated assets of insolvent insurers and preserving jobs at troubled insurance companies. CDI's experiences in California have also enabled the Department to provide national leadership in the area of conservation and liquidation.

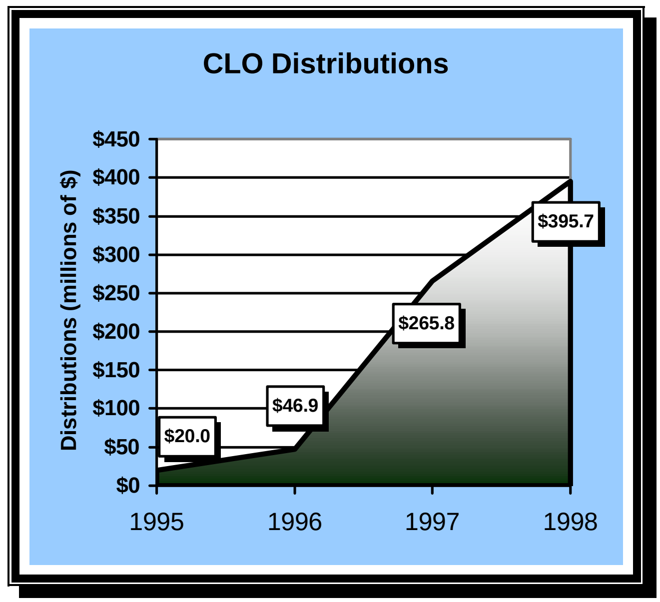
## *Restoring the Conservation and Liquidation Office*

By the end of 1994, CDI's Conservation and Liquidation Office (CLO) had been the subject of three management audits, numerous legislative hearings and extensive investigative reports by the media across California. CLO had developed a reputation for failing to safeguard the assets of those who were insured by bankrupt insurance companies under state supervision. *The Sacramento Bee* ran a three-part series on the serious mismanagement of assets by the CLO, including "private auctions" of conserved company assets to state employees at discount prices.[84]

From 1995 through 1998, CDI has worked to transform the CLO into a model of how to manage the affairs of conservations and receiverships in California for the benefit of its claimants. Today, the CLO is maximizing its available resources to protect consumers who were shortchanged by their bankrupt insurance companies and has become one of the premier receivership operations in the country.

From 1995 to 1997, the CLO closed 34 insolvent estates in just two years compared to 29 cases closed during the previous four years. Between 1995 and 1998, CLO assisted policyholders in recovering nearly $730 million from insurance companies, returning $395.7 million in 1998 alone.[85] *Exhibit 26* summarizes the amount of distributions returned to consumers.

***Exhibit 26: Conservation and Liquidation Office Distributions***




Source: California Department of Insurance, Conservation and Liquidation Office, 1999.

### Early Warning System

The *Early Warning System* is an instrumental tool in CDI's policyholder protection effort. CDI's internal resources have been strengthened for analyzing the fiscal health of insurers, providing valuable lead-time for CDI to intervene and protect the interests of consumers before viability concerns become critical.

CDI has also enhanced its financial surveillance through increased staffing of the *Troubled Companies Unit* and providing staff training to develop more comprehensive automated analytical tools to diagnose the financial condition of insurers.

[84] *Sacramento Bee*, February 20-22, 1994.

[85] California Department of Insurance, Conservation and Liquidation Office, 1999.

These strengthened monitoring efforts are working; the number of insolvencies has decreased from 112 in 1995 to 69 today.

## A Case Study

Through more effective operations within the CLO, CDI has protected the interests of policyholders. For instance, on January 31, 1997 CDI seized one of the state's largest writers of workers' compensation insurance, to protect its policyholders from unsafe management practices.[86] The insurance company had attempted to conceal the true financial condition of the company from CDI's financial examiners. In September 1996, a CDI investigation discovered that the company was under-reserved by $138.5 million and was in imminent danger of collapsing. The company's demise would have left thousands of consumers unprotected.

Within four months, CLO seized the company, stabilized it, sold it and put it back into the private sector under new management.[87] Not only did policyholders benefit from this action, but it also saved over 1,200 jobs in San Diego. The company has now been rehabilitated and is again operating as a viable going concern.

## National Leadership on Insurer Insolvency Issues

The experiences in California have made CDI a national leader in solvency screening. California, along with a handful of other states – New York, Ohio, Pennsylvania, and Texas – have developed sophisticated approaches to protect consumers against insurer insolvency.[88] CDI also actively participates on committees and task forces of the NAIC to enhance insurance regulators' ability to promote and protect the solvency of insurance companies:[89]

- **Accounting Practices and Procedures Task Force** – Identifies, investigates, and develops solutions to accounting problems with the goal of guiding insurers in properly accounting for various aspects of their operations. Modifies the *Accounting Practices and Procedures* manuals to reflect changes necessitated by task force action and studies innovative insurer accounting practices that affect the ability of regulators to determine the true financial condition of insurers. This task force has overseen a complete re-codification of statutory accounting principles (SAP) and the establishment of a comprehensive process to maintain SAP.
- **Risk Based Capital Task Force** – Evaluates and recommends appropriate refinements to capital requirements for all types of insurers.
- **Special Insurance Issues Committee** – Addresses special issues relating to miscellaneous lines of insurance such as title, surety, fidelity, mortgage, and reinsurance.
- **Valuation of Securities Task Force** – A forum for proposed changes or interpretations of the *Purposes and Procedures of the Securities Valuation Office*. This document governs how the SVO staff values securities and constitutes the task force's permanent instructions to the staff on valuation matters. Reviews new investment vehicles being purchased by insurers and provides appropriate annual statement disclosure, credit evaluation techniques, and valuation methods.
- **Special Committee on Financial Services Modernization** – Addresses issues related to regulating the insurance activities of banks and other entities that offer a mixture of financial/insurance products in the US.
- **Casualty Actuarial Task Force** – Identifies, investigates and develops solutions to actuarial problems in the property and casualty insurance industry to maintain the financial health of property and casualty insurers.
- **Life and Health Actuarial Task Force** – Identifies, investigates, and develops solutions to actuarial problems in the life and health insurance industry to maintain the financial solvency of life and health insurers.

# *Innovative De-mutualization Efforts*

Nationally, about 100 of the nation's 1,200 life insurance companies are organized and operate as what is referred to as *mutuals*, but this handful of companies issue approximately one-third of the 195 million individual life insurance policies in force and the same proportion of the industry's $346 billion in assets.[90] Legislation to allow de-mutualization has been enacted in California, as well as 15 other states and Washington, DC. During the period of 1995 to 1998, CDI oversaw the de-mutualization of an

[86] California Department of Insurance, Press Release #050, June 2, 1997.
[87] *Insurance Commissioner of the State of California vs. Golden Eagle Insurance Company*, Case No. 984502, Superior Court of the State of California for the County of San Francisco, February 4, 1998.
[88] Klein, Robert W., "Structural Change and Regulatory Response in the Insurance Industry," June 19, 1995.
[89] National Association of Insurance Commissioners, 1999 Committee List: Committee, Subcommittee, and Task Force Assignments, January 27, 1999.
[90] New York State Assembly, Standing Committee on Insurance, Alexander B. Grannis, Chair, March 1998.

insurance company which was then the largest mutual life insurer in California.

"De-mutualization" refers to a mutual life insurer (i.e. an insurer that is mutually owned by its policyholders) that is converting to a stock company. To convert, each individual policyholder's interest must be accurately calculated and a distribution of that value must be effected. This distribution could take the form of stock transfers, cash, or credits to policyholders. De-mutualization gives life insurers greater organizational flexibility and ready access to capital in an era of consolidation and increasing competition from banks, mutual funds, and other sectors of the financial services industry. Consumers can potentially reap tremendous benefits from de-mutualization by receiving equity in the newly reorganized insurer and by the superior financial footing of the insurer.

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# INTERNATIONAL EFFORTS FOR HOLOCAUST SURVIVORS

CDI was instrumental in launching an international initiative to compensate Holocaust survivors on unpaid insurance claims. Helping to create and working within the International Commission on Holocaust Era Insurance Claims (ICHEIC), CDI is leading efforts to obtain settlements from European insurance companies that have denied life insurance claims to an estimated 20,000 or more Holocaust survivors and their heirs living in California.

## Holocaust Background

In the 1930's and 40's insurance was sold extensively throughout Europe, primarily to the middle and working class. Many people invested their money in life insurance policies and in annuities because retirement planning accounts, such as pensions, were not widely available.

As the religious and political oppression preceding World War II spread, and later, as the war and Holocaust enveloped Europe, more and more people purchased insurance products in an effort to secure their assets for when and if they survived. In fact, insurers offered, for extra premium, policies that would pay in "New York Dollars" because of the stability offered by U.S. currency and the rampant instability of the various European currencies at the time.

## 50 Years Later

Today, over 50 years after the Holocaust, a large number of survivors and heirs in California, and internationally, are making public the disgrace of insurers for not paying on legitimate claims of Holocaust victims. An estimated 50,000 to 100,000 Holocaust survivors currently live in the United States. Second only to New York, California is the resident state of the largest number of survivors, at approximately 20,000. A rough estimate of heirs and beneficiaries could easily bring the total of descendents to three to four times these numbers.

Although survivors and heirs are stepping forward with insurance policies, policy numbers, cancelled checks, and other proof of insurance coverage to recover their benefits, in most cases such proof has not been sufficient for the insurance carriers to pay what is rightfully owed to them.[91]

Insurers claim they are no longer responsible for paying these claims for a variety of reasons: *no death certificate was provided by the claimant; policyholders stopped making premium payments during the war; proceeds of policies sold to Jewish insureds were already paid to the Nazis; reparations to Holocaust survivors were made by the government restitution treaties, which covered insurance proceeds; companies located in eastern-bloc countries were taken over by communist regimes and their assets were confiscated so that no funds exist to pay claims; records no longer exist to verify the individual's status as a policyholder beneficiary*. It is true that in some instances, research must be performed to verify the legal position of the company. The basic point, however, is that an insurance policy is an exchange of promises; the insured policyholder promises to pay a premium in exchange for the promise by the insurer to pay benefits once the insurance policy conditions are met.

CDI has taken the position that in most cases the insurers' defense for not paying these claims is unacceptable, and transgresses even the simplest notion of ethical treatment of Holocaust survivors. The difficulties encountered by an insurance company do not negate the promises sold through insurance policies. Moreover, many of the companies were located outside Germany and had their property returned by eastern bloc countries. Hitler and the Third Reich did not issue death certificates as they massacred millions of people. Nazis seized family assets, including their insurance policies along with the rest of their possessions. Most survivors were fortunate to leave Europe alive and to expect them to have kept policies, receipts, documentation, or other personal belongings while fleeing is simply unrealistic. Likewise, premium payments could not be made while policyholders were held in concentration camps.

## *The Significance of this Effort*

This effort reflects CDI's unwavering commitment to protect the interests of residents of the State of California and ensure that the insurance companies operating in California are fulfilling their promises and contractual obligations.

Also of consideration is the world community, especially the Jewish community, who suffered the greatest loss from the appalling acts of genocide during World War II. Long overdue, these efforts to reimburse Holocaust claimants may help to restore goodwill and trust between survivors and the State of California.

[91] California Department of Insurance, *Budget Change Proposal*, 1999, p 3.

## *California's Responsibility to Restore Benefits for Holocaust Survivors*

CDI is charged with protecting the rights of the residents of California. The vision, mission, goals, and function of the CDI all promote fairness, which is the fundamental core value of CDI. This effort exemplifies the reason that CDI exists. More importantly, the California Department of Insurance upholds a moral obligation to rectify a grievous historical wrong where it has the power to do so.

California law clearly states that the Insurance Commissioner must protect the rights of California's residents as expeditiously as possible. By taking aggressive action, CDI can ensure that insurance companies are held accountable to pay legitimate benefits to all surviving victims and heirs of the Holocaust who currently reside in California.

If these policies were paid today at present value, with currency adjustments and interest, the total due could reach into the hundreds of millions or even billions of dollars. Many of the claimants have insurance policies and policy numbers. Most claimants were children during the war, and many are certain that their parents and relatives had insurance because they recall the agent coming to their home for payment. The majority of claimants have no actual knowledge of whether or not their family members were insured, but believe they did because of their social and economic status at the time or because of their parents' business holdings.

### What Has Been Done So Far

In November 1997 and January 1998, CDI held three public investigatory hearings in Los Angeles and San Francisco to collect information and evidence regarding unpaid insurance claims owed to survivors of the Holocaust. At those hearings, the Commissioner heard disturbing testimony from survivors who were adults during the war, survivors who were children during the war, claimants born in the U.S. whose parents and grandparents perished in concentration camps and historians and insurance researchers. The purpose of the hearings was to collect testimony and information, publicize the issue for claimants who might need help collecting information to prove their claim and to hear testimony from some of the insurers involved. The hearings also served to heighten awareness of the general public on the issue.

### The International Commission on Holocaust Era Insurance Claims

CDI was the stimulus in establishing the International Commission on Holocaust Era Insurance Claims (ICHEIC). The ICHEIC's mission is to:

*(a) Secure records and archives*

*(b) Establish funding for the payment of claims*

*(c) Set parameters and standards of proof for claims*

*(d) Identify survivors and/or their heirs*

*(e) Facilitate the payment of legitimate life and property claims on unpaid WWII era insurance policies.*

Through the ICHEIC, several of the largest insurers that have unpaid policies from WWII have pledged to pay claims as directed by the ICHEIC. In April 1998, these insurers signed a *Memorandum of Intent* that marked the beginning of the first real possibility of bringing closure to the insurance-related issues of this shameful period in history. In addition, these insurers have pledged to dedicate funds that will compensate survivors whose policies were paid to the Nazis, those whose policies were confiscated by communist governments after the war, or who have no actual proof of having a policy but believe that such policies were in effect. At the November 1998 meeting of the ICHEIC in London, England, the insurers pledged $90 million as an initial payment to humanitarian funds and an additional $5 million for an administrative expense to fund the activities of the ICHEIC.[92]

### CDI's Leadership Role

CDI is committed to carrying out the program in an effective and timely manner. The ICHEIC has agreed to complete its work within two years so that the aging survivors may be compensated during their lifetime and closure can be brought to the restitution issue for all concerned. This is a relatively short time frame to manage such a legally, financially and emotionally complicated issue. CDI is committed to requiring insurance companies to uphold their respective obligations and bring a quick and effective resolution to this process. This multi-faceted program includes the following components:

- Notices to Insurance Companies – Insurance companies that conduct business in California to receive letters formally requesting that they inform CDI whether, they, or any of their present of former affiliated companies, issued policies in Europe prior to World War II, and whether they will participate in the International Commission for Holocaust-Era Insurance Claims.
- California Holocaust Insurance Settlement Alliance – A 28-member alliance will mount a massive outreach effort to help identify Holocaust survivors and heirs who might be entitled to insurance restitution.

[92] California Department of Insurance *Budget Change Proposal*, 1999, p. 8.

- Print Ad – A comprehensive advertising program, designed to increase awareness among Holocaust survivors and heirs, will include advertisements in nearly 30 general-circulation newspapers and Jewish publications throughout the state.
- Mailings to Survivors/Heirs – Holocaust survivors and heirs statewide are to receive letters and restitution application forms.
- 888 Toll Free Number – CDI will offer a toll free number—888 CDI-INFO (888/234-4636) dedicated solely to potential Holocaust insurance claimants.
- Web Site – An update of the CDI Website *(www.insurance.ca.gov)* will include a claim form for survivors and heirs, history on Holocaust restitution efforts, and information on companies that have failed to pay Holocaust insurance claims.

## Settlements for Holocaust Victims

CDI has led efforts to obtain settlements from insurance companies who benefited from Holocaust victims. Various Holocaust lawsuits are taking place across the nation in both state and federal courts to recover funds for Holocaust survivors and heirs.

Several of these Holocaust lawsuits are currently taking place in the State of California. The following lawsuits were filed in California on behalf of Californian residents, claiming wrongful denial of Holocaust victims' claims:

- *Babos v. Assicurazioni Generali SpA et al.*
- *Friedman v. Assicurazioni Generali SpA et al.*
- *Sladek v. Assicurazioni Generali SpA et al.*
- *Stern v. Los Angeles Superior Court*
- *Stahl v. Victoria Holding, Assicurazioni Generali SpA et al.*

In addition, a class action suit, *Cornell v. Assicurazioni Generali, et al.*, was filed in Federal District Court in New York on behalf of Holocaust victims and their heirs and beneficiaries. The lawsuits name approximately 15 insurer defendants who are affiliates of international insurance conglomerates, many of which directly or through affiliates do substantial business in California. CDI will continue to monitor the litigation closely and assist the plaintiffs' counsel, as appropriate, to protect the interests of California residents.

CDI intends to also defend the constitutionality of the recently enacted California legislation, calling for the extension of the *Statutes of Limitations* and other provisions enacted to protect the rights of these claimants.

## Holocaust Restitution Efforts

CDI vigorously supported SB 1530 (Chapter 963/Sept. 1999)– legislation that provides $4 million to fund outreach efforts in identifying and collecting data on Holocaust victims and their heirs. These funds are being used to develop and implement a coordinated approach to gather, review and analyze the archives of select insurance groups and other archives and records using onsite teams and an oversight committee with expertise in accounting, law, insurance archaeology, economics, and public information.[93] These experts in their respective disciplines will provide research and investigation into insurance policies, unpaid insurance claims, and related matters of Holocaust victims and their beneficiaries or heirs. In addition, they will analyze losses arising from the activities of the Nazi-controlled German government or its allies for insurance policies by insurers who have affiliates or subsidiaries authorized to do business in California.

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[93] California Department of Insurance, Press Office, "Unpaid Insurance Claims of Holocaust Victims—Timeline", undated.

# HELPING URBAN COMMUNITIES

CDI has been a proven leader in identifying problems in the insurance market and developing innovative ways to solve those problems for California's consumers. For example, in the last four years, CDI implemented new methods to address the problem of availability and affordability of insurance in urban areas and encourage the active participation of the insurance industry in an innovative statewide program to promote fire safety.

## *Efforts to Spur Insurance Involvement in Urban Areas*

CDI is committed to providing greater access to insurance coverage for those communities that historically have been under-served and under-insured. The main criteria for identifying an under-served community include a high-uninsured motorist rate, high minority percentage, and low per-capita income. Promoting more involvement in communities long neglected by the insurance industry has become a staple of CDI's management direction. In this effort, CDI is calling on industry and community groups to participate in an outreach program targeted at California's under-served communities. Many people in these communities do not have adequate access to information about insurance. They've never been told why it's important, what its real costs are, and what their options are with respect to coverage and company selection.

## *The Commissioner's Report on Under-served Communities*

CDI initiated several studies on under-served communities to accurately measure the special needs and dynamics of that segment of society. The results of these studies are contained in the *Commissioner's Reports on Under-served Communities*. This has led to efforts to address the following important issues:

- In 1995, 151 zip codes were under-served.
- Approximately 6% of all private passenger auto insurance in California was sold in under-served communities.
- Only 4-5% of insurance agents or service offices are located in under-served communities – considerably lower than the approximately 16% of people who live in under-served communities.
- Only about 6% of total solicitations by mail were made to under-served communities.[94]

These reports represent an important step in assessing the insurance industry's participation in all California communities. In fact, a number of insurers have already initiated programs to increase their participation in under-served communities. Future reports will be a useful tool in evaluating the success of these programs.

CDI believes that it must take a proactive role in making information about insurance more available to those individuals living in under-served communities. In order to ensure these efforts receive consistent attention, CDI created the External Affairs and Policy Branch—the main purpose of which is to serve as an advocate and agent for individuals and communicates historically disconnected from the insurance industry. CDI's studies indicate that many residents of high-uninsured communities have little information about insurance. The average uninsured tends to be much more disconnected from the insurance system and typically does not engage in efforts to obtain insurance. CDI, the insurance industry, and other community-based organizations must take advantage of opportunities to fill the information void.

## *California Organized Investment Network*

In February 1996, CDI established the **California Organized Investment Network** (COIN) to facilitate insurance industry investments in California communities in need of economic development or low-income housing. Since its inception, the COIN program has worked to increase the level of insurance industry capital committed to sound investments for economic development and affordable housing benefiting California's low to moderate income urban and rural communities.

COIN was initially conceived as a three-year voluntary pilot program in place of a proposed legislative mandate requiring the insurance industry to either report annually about community development investments or to invest a percentage of premium revenues into investments benefiting low-and moderate-income communities.

[94] California Department of Insurance, Statistical Analysis Bureau, 1996 Commissioner's Report on Under-served Communities.

COIN's primary purpose is to help insurers identify investment opportunities in under-served communities. These investments may include municipal bonds, commercial property acquisitions, low-income housing tax credit funds and direct investments in financial intermediaries. COIN has also devised numerous tools, such as the *Investment Policy*, *Investment Bulletin*, *Impact Capital,* and the *Product Committee* that help the insurance industry "discover" opportunities previously overlooked.

Since its beginning, COIN's remarkable success exceeded expectation – **the insurance industry has voluntarily invested over $260 million in a variety of projects, including more than $144 million in 1998 alone**.[95] COIN has been such a success that many other states, such as Missouri, New York, Louisiana, and Massachusetts, are using it as a model for their efforts to boost insurance investment in under-served communities.

Embedded in COIN's success is its ability to help community organizations understand what types of investments are made by insurers and help insurers understand that simply looking at traditional "Wall Street" investment vehicles can often ignore a whole world of safe, yet rewarding investments in California's communities. COIN has also been successful in stimulating dialogue within the insurance industry regarding innovative ways to invest in under-served communities.

> *"Commissioner Quackenbush's leadership in this important area is admirable. When the final two reports are finalized, we will have a three-year profile to reference that will enable us to precisely assess how well companies have worked to increase access to insurance products to people in under-served communities over that three-year time span."*
>
> ***—Andrew Ysiano, President***
> *California Hispanic Chamber of Commerce*

Despite these early successes, CDI intends to vigorously pursue those companies that have not responded to the initial efforts. CDI must continue to focus its attention on working with companies to effectively provide access to insurance products to people in under-served communities.

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[95] California Department of Insurance, News Release, "Insurance Commissioner Releases First-Ever Report on Under-served Communities".

# APPENDIX

## *Exhibit 27: Information Technology Achievements, 1995 - 1998*

| MAJOR INFORMATION TECHNOLOGY ACHIEVEMENTS, 1995 - 1998 | | |
|---|---|---|
| ***Then (1995)*** | ➔ | ***Now (1998)*** |
| ▪ No departmental review or prioritization of IT resources.<br>▪ Not aligned with CDI priorities. | ➔ | ▪ *IT Policy Committee* prioritizes IT projects CDI-wide at Executive management level. |
| ▪ No method to document, analyze, estimate requests for IT services. | ➔ | ▪ *IT Service Request Process*: aligns IT resources with CDI priorities. |
| ▪ Network was not stable, frequently not available.<br>▪ Loss of work production. | ➔ | ▪ Predictable and stable LAN. |
| ▪ No consistency in configuration and no standard equipment. | ➔ | ▪ Standard configuration of LAN and WAN, all staff working off standard application software.<br>▪ Fewer resources are required to maintain, lower training and maintenance costs, better exchange of documents among staff. |
| ▪ No internet/intranet.<br>▪ High postage and mailing costs. | ➔ | ▪ CDI internet/intranet. Higher level of customer service and satisfaction.<br>▪ Public has assess to more consumer data. |
| ▪ No standard case tracking documentation.<br>▪ No standard timekeeping or management reporting. | ➔ | ▪ Fraud investigator Case Management System. Implemented fraud investigator case management application with auto link to TARS.<br>▪ Implemented case tracking and timekeeping automation for Financial Analysis Division and launched CDI-wide case tracking project.<br>▪ Converted Policy Tracking from Forms 3.0 to 4.5, with additional reports. |
| ▪ No electronic filing capability or nationwide producer database. | ➔ | ▪ Currently undertaking initiatives to reduce costs, align CDI with industry standard and shorten approval process<br>▪ Piloted ***System for Electronic Rate and Form Filing*** (SERFF) standard.<br>▪ Made processing improvements licensing system and working toward moving licensing application to IDB.<br>▪ **PDB/PIN**: Industry standard electronic transaction processing |
| ▪ High telecommunications costs. | ➔ | ▪ Reduced telecommunications costs by 60%. Consolidated telecommunications administrative services.<br>▪ Call tracking implemented at all sites.<br>▪ Reduced videoconference costs.<br>▪ Prop. 103: call center menu structure revised. |
| ▪ Manual work processes. | ➔ | ▪ Automated budgeting and accounting processes.<br>▪ Automated Legal Division processes. |

Source: California Department of Insurance, Administration Division, 1999

*Exhibit 28: Administrative Systems Achievements, 1995 - 1998*

| Major Accomplishments, Administrative Systems, 1995-1998 | | |
|---|---|---|
| ***Then (1995)*** | ➔ | ***Now (1998)*** |
| ▪ No cost accounting mechanisms to accurately capture the time and expense devoted to reimbursable activities. As a result, such activities would have to be funded from limited fee and license revenues. Also, unable to validate reimbursement rates set by the CDI. | ➔ | ▪ Implemented a Time activity Reporting System to capture data related to reimbursable activities and to facilitate a formal rate validation process. |
| ▪ No standard billing system to track proper billing of CDI's services and to accurately record receipts. | ➔ | ▪ Implementation of Oracle Financials – Accounts Receivable System and ACCESS reporting. |
| ▪ Duplication of time entry by program employee resulted in inaccurate program cost reporting. | ➔ | ▪ Incorporated CSD and FAD Case Tracking System in TARS. |
| ▪ Highly technical CALSTARS financial reports were difficult for managers to comprehend and use effectively. | ➔ | ▪ Electronically downloaded CALSTARS data using Monarch and reformatted to ACCESS to provide more understandable financial reports. |
| ▪ Inaccurate cost allocation system and misallocated expenditures to programs. | ➔ | ▪ Revamped cost allocation system to reflect allocation based on actual costs and include regular reviews and updates. |

Source: California Department of Insurance, Administration Branch, 1999

*Exhibit 29: Human Resources Management Achievements, 1995 - 1998*

| Major Accomplishments, Human Resources, 1995-1998 | | |
|---|---|---|
| ***Then (1995)*** | ➔ | ***Now (1998)*** |
| ▪ CDI provided "free" loans to employees. For example, one employee received $10,000 in salary advances with $100 monthly payback. | ➔ | ▪ Enforce strict adherence to State Administrative Manual (S.A.M.) procedures regarding salary advances. |
| ▪ Employees routinely received and cashed paychecks early. | ➔ | ▪ Enforce strict adherence to S.A.M. regarding release of paychecks. |
| ▪ Lack of security in Human Resources Management Bureau (HRMB). | ➔ | ▪ Relocated HRMB to secure location in accordance with State Controller's Office (SCO) requirements. |
| ▪ Employees were being overcompensated for working out-of-state by as much as $200 to $500 per month per employee. | ➔ | ▪ Enforce strict adherence to Department of Personnel Administration (DPA) rules regarding out-of-state compensation. |
| ▪ Attendance rules were not uniformly or appropriately applied.<br>▪ Attendance and leave balances were not kept up to date, thus creating overpayments.<br>▪ Employee attendance summaries (Form 634) were not completed for employees.<br>▪ "Late docks" were not reported in a timely manner. | ➔ | ▪ Established attendance recording and reporting procedures.<br>▪ Provide training to attendance monitors.<br>▪ Established procedures to ensure Form 634 were returned to HRMB on a timely basis. |
| ▪ CDI had staff positions misclassified, inaccurately compensating some staff for work performed. | ➔ | ▪ Corrected the misclassifications. |
| ▪ Disciplinary actions were not taken. | ➔ | ▪ Training for managers and supervisors.<br>▪ Aggressive follow-up to ensure appropriate disciplinary actions is taken. |
| ▪ Appointment and certification were not implemented properly. | ➔ | ▪ Utilize State Personnel Board's (SPB) on-line certification.<br>▪ Developed policies and procedures to ensure exams and certifications are conducted in accordance with SPB rules. |
| ▪ Backlogged merit awards. For example, two employees submitted merit suggestions in February 1980. The suggestions were implemented but the employees did not receive their merit awards until February 1996. | ➔ | ▪ Eliminated backlog. |
| ▪ Employees were separating from CDI without proper clearance. Some owed CDI money or equipment. | ➔ | ▪ Established separation process. |
| ▪ CDI was not in compliance with DPA rules requiring each department to establish Substance Testing Program for sensitive position. | ➔ | ▪ Established Substance Testing Program. |
| ▪ Managers and supervisors were not familiar with State's civil service hiring process resulting in illegal or inappropriate appointments. | ➔ | ▪ Instituted civil service hiring policies and procedures.<br>▪ Train managers and supervisors.<br>▪ Developed handbook on Civil Service Process. |
| ▪ Employee performance appraisals were not done timely or properly. | ➔ | ▪ Provide training to managers and supervisors.<br>▪ Established tracking and monitoring system to remind managers and supervisors to complete appraisals. |
| ▪ CDI was not in accordance with DPA rules on sick leave administration. | ➔ | ▪ Enforce strict adherence to DPA rules.<br>▪ Issued HRMB Bulletin reminding managers and supervisors of their responsibility to properly administer sick leave usage. |
| ▪ Job injuries were not reported in a timely manner and managers and supervisors were not familiar with the reporting process. | ➔ | ▪ Established written procedures and "information kit" to assist managers and supervisors.<br>▪ Provide training to managers and supervisors. |

*Exhibit 29: Human Resources Management Achievements, 1995 – 1998 (continued)*

| Major Accomplishments, Human Resources, 1995-1998 | | |
|---|---|---|
| ***Then (1995)*** | ➔ | ***Now (1998)*** |
| ▪ CDI did not have established policies on discrimination and sexual harassment in compliance with EEO regulations. | ➔ | ▪ Developed "Zero Tolerance" Statement and Policy Manual specifically addressing discrimination and sexual harassment.<br>▪ Posted policies and procedures on CDI intranet.<br>▪ Policies and procedures were emailed to every CDI employee.<br>▪ Policies and procedures are provided in the orientation packet for new employees. |
| ▪ CDI had no communication between EEO, labor relations, and adverse action functions of the HRMB. Cases often overlapped in terms of disability, workers' compensation, and general medical.<br>▪ Adverse actions were not always adequately analyzed. | ➔ | ▪ Established Return to Work Council as required for each state agency.<br>▪ Council members – Classification and Compensation Manager, labor relations manager, and the EEO manager meet on monthly basis to review cases and apply regulations from their respective areas to bring resolution.<br>▪ A Return to Work Procedures Guide was developed. |

Source: California Department of Insurance, Administration Branch, 1999

*Exhibit 30: Accounting Office Achievements, 1995 - 1998*

| Major Accomplishments, Accounting Office, 1995-1998 | | |
|---|---|---|
| ***Then (1995)*** | ➔ | ***Now (1998)*** |
| ▪ Incumbent accounting staff did not have the necessary background, education, CALSTARS experience, or other work experience to perform proper accounting functions.<br>▪ Inefficient and deficient accounting operation. | ➔ | ▪ Hired qualified and professional staff with necessary background.<br>▪ Provide training.<br>▪ Centralized accounting operation. |
| ▪ Insufficient staffing to meet workload demands.<br>▪ Reliance on regular use of student assistants. | ➔ | ▪ CDI received legislative approval to add nine positions to Accounting Office in FY 1999/2000. |
| ▪ Inadequate or ineffective communications within the accounting operations.<br>▪ Fragmented and incoherent operations. | ➔ | ▪ Accounting management and supervisors have implemented regular communications between staff and accounting units. |
| ▪ Monthly reconciliation of the State Controller's records and CDI's CALSTARS reports were not done in a timely fashion.<br>▪ Inaccurate accounting reports / balances. | ➔ | ▪ Monthly reconciliations are completed in a timely manner and are completed with accuracy and in compliance with the SAM requirements. |
| ▪ Revolving Fund was out of balance by $1.2 million (account totaling $3 million) due to unresolved items dating back 15 years.<br>▪ Revolving Fund inaccuracies placed limitations on amount available to CDI. | ➔ | ▪ A three-year project resulted in the identification and resolution of all unresolved items in the Revolving Fund.<br>▪ All unresolved items are not reconciled on a monthly basis. |
| ▪ Over 200 unidentified receipts totaling $250,000 were residing in the uncleared collections account were not processed and cleared. | ➔ | ▪ All unresolved items in the uncleared collections account have been researched, validated, and cleared.<br>▪ Unresolved items are now reconciled on a monthly basis. |
| ▪ No standardized billing system to track proper billing of CDI's services.<br>▪ Lack of system to follow-up and accurately record receipts. | ➔ | ▪ Implemented Oracle Financials Accounts Receivable System to consolidate departmental billings and provide for automated generation of follow-up letters. |
| ▪ Uncollectable account receivables totaling $5.3 million and dating back to the early 1980's were not written off and cleared from CDI's records. | ➔ | ▪ All uncollectable receivables have been written off and cleared from CDI's books.<br>▪ Account receivables are regularly monitored and cleared. |
| ▪ Six-week backlog in cashiering operations.<br>▪ Checks for issuance of licenses were not deposited in a timely manner.<br>▪ Cashiering functions were performed inefficiently with unreliable and antiquated cashiering system dating back to the 1960's.<br>▪ Lack of automated processing resulted in manual and redundant workloads. | ➔ | ▪ Additional resources were added, reducing the backlog to less than two days.<br>▪ Cashiering system was redesigned, including the acquisition of a remittance processor, allowing expanded capabilities.<br>▪ Workload automated eliminating redundant activities. |
| ▪ CDI's invoices for products and services were not being paid timely or accurately. | ➔ | ▪ Additional staff and proper training have resulted in more timely and accurate payment of CDI invoices. |
| ▪ Lack of internal control of travel advances.<br>▪ Employees permitted to accumulate travel advances without regular reimbursement. | ➔ | ▪ Internal procedures have been implemented to ensure proper issuance of travel advances and the collection of reimbursements from employees. |

Source: California Department of Insurance, Administration Branch, 1999

*Exhibit 31: Budget Office Achievements, 1995 - 1998*

**Major Accomplishments, Budget Office, 1995-1998**

| Then (1995) | ➔ | Now (1998) |
|---|---|---|
| ▪ Program managers were not responsible for managing their respective budgets. | ➔ | ▪ CDI has adopted a policy of holding program managers accountable for managing their budgets. |
| ▪ Managers did not receive information on their annual budget allotments or expenditures impacting their budgets. | ➔ | ▪ Budget allotments are issued shortly after the state budget is enacted. Allotment briefings are provided to each Deputy Commissioner. |
| ▪ Budget reports did not match departmental appropriations. | ➔ | ▪ Implemented monthly reconciliation of budget allotments to departmental appropriations. |
| ▪ Expenditure reports were not accurate due to improper coding of expenditures. | ➔ | ▪ A new expenditure-coding manual was developed.<br>▪ Expenditure Training is provided. |
| ▪ Program staff did not know how to prepare budget change proposals (BCP) to justify their budget requests. | ➔ | ▪ Budget instructions are issued each year to program staff during budget development process.<br>▪ Annual on-site training is provided. |
| ▪ Money received by CDI was not separately identified by source and use. | ➔ | ▪ Revenue is tracked by source.<br>▪ Cost distribution report was developed to monitor expenditures to corresponding revenue sources. |
| ▪ Proposition 103 assessments and examination rates were not calculated in a timely manner. | ➔ | ▪ Assessment and rates are calculated shortly after enactment of annual budget. |
| ▪ No process in place to monitor billings for examination reimbursement to ensure full recovery of costs. | ➔ | ▪ Program managers are responsible for verifying the accuracy of billable hours in TARS.<br>▪ A monthly report comparing billable hours to those billed and those recorded in TARS is provided to program managers. |
| ▪ Lack of cash flow management resulted in insufficient money to fund operations or inability to fund contingencies. | ➔ | ▪ A monthly cash flow analysis is conducted to ensure revenues are being collected to support expenditures. |
| ▪ Audits conducted by the Department of Finance, the State Controller's Office, and the Bureau of State Audits identified serious fiscal management deficiencies in CDI.<br>▪ CDI lacked systems, controls, or procedures to properly monitor and manage its revenues and expenditures.<br>▪ Deficiencies, combined with two related lawsuits, depleted the Insurance Fund requiring a General Fund loan of $14 million and staff layoffs of 94 positions, including 60 in consumer protection programs. | ➔ | ▪ CDI's financial operation was restructured to ensure coordination and control over all aspects of financial management.<br>▪ A formal budget management process was implemented to make program managers responsible for monitoring their revenue collections and expenditures.<br>▪ General Fund loan was repaid, Insurance Fund reserves were established for contingencies, and all staffing reductions have been restored, including a substantial increase in consumer protection staffing. |

Source: California Department of Insurance, Administration Branch, 1999

***Exhibit 32: Business Services Management Bureau Achievements, 1995 - 1998***

| Major Accomplishments, Business Services Management, 1995-1998 | | |
|---|---|---|
| ***Then (1995)*** | ➔ | ***Now (1998)*** |
| ▪ Antiquated inventory control system. | ➔ | ▪ Implemented bar coding system. |
| ▪ Inaccurate inventory records. | ➔ | ▪ Conducted statewide inventory. |
| ▪ Inadequate security of CDI offices. | ➔ | ▪ New card key system installed. |
| ▪ No risk analysis for department data services. | ➔ | ▪ Filled Information Security Officer (ISO).<br>▪ Conducted risk analysis. |
| ▪ Record retention schedules out of date. | ➔ | ▪ Increased staff and updated schedules. |

Source: California Department of Insurance, Administration Branch, 1999